

Islamic Economic Series—2

Ethics and Economics

An Islamic Synthesis

SYED NAWAB HAIDER NAQVI

Dedicated

to

ANDALIB, TAHMINA, QURRATULAIN
AND NEELOFAR

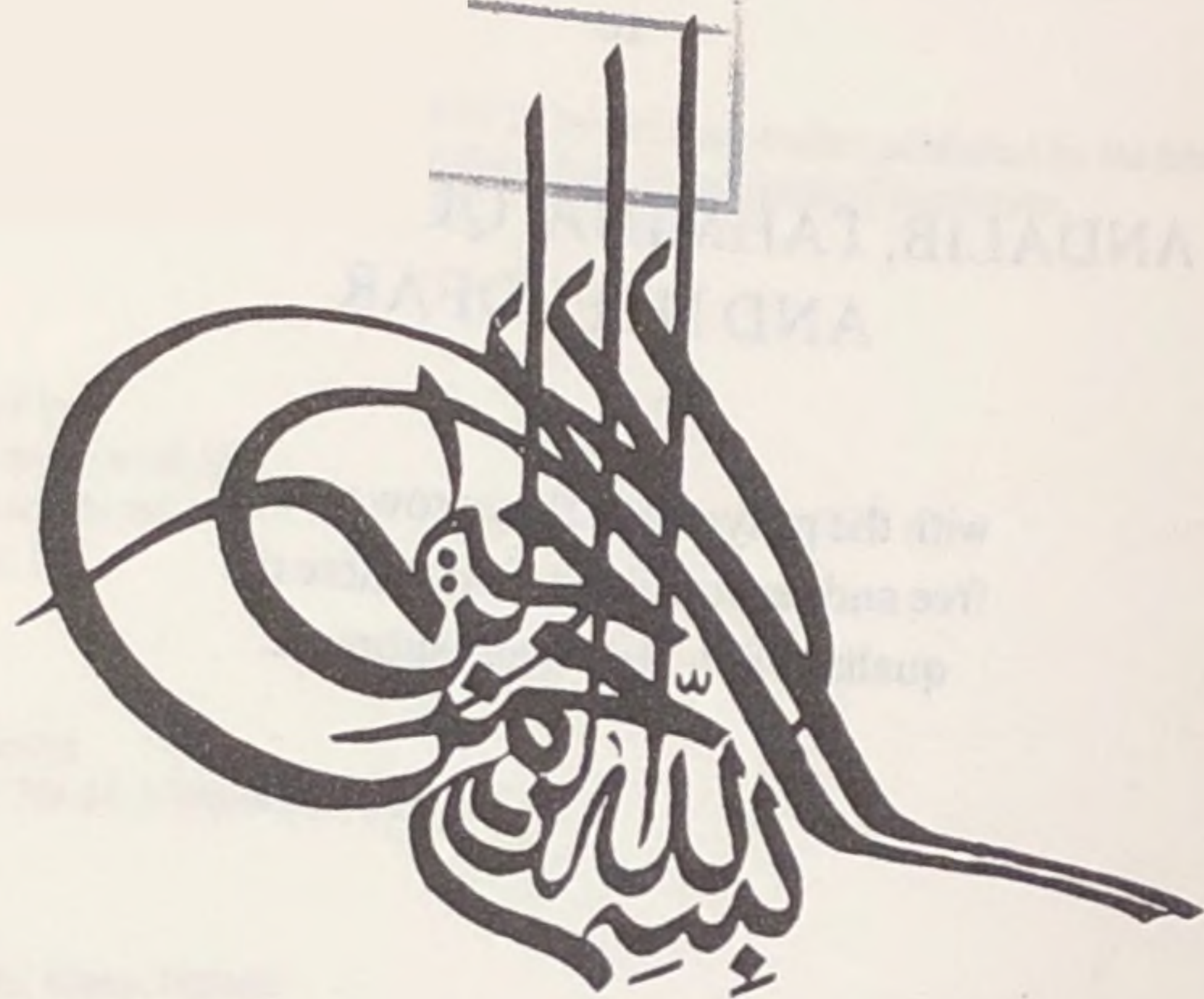
with the prayer that they grow up in a
free and responsible world, where the
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IN THE NAME OF ALLAH,
THE MERCIFUL,
THE MERCY-GIVING

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بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

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وَنَجْعَلَهُمْ أَئِمَّةً وَنَجْعَلَهُمُ الْوَارِثِينَ ۖ وَنُكَفِّرُ لَهُمْ فِي الْأَرْضِ

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“AND WE DESIRED TO SHOW FAVOUR UNTO THOSE
WHO WERE OPPRESSED IN THE EARTH, AND TO
MAKE THEM EXAMPLES AND MAKE THEM THE
INHERITORS, AND TO ESTABLISH THEM ON
EARTH...” THE HOLY QUR’ÂN (28:5–6)

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Foreword

The contemporary Muslim world is passing through one of the most critical yet creative periods of its history. Despite political freedom and economic resilience the pattern of life imposed upon Muslims during the period of colonial rule and strengthened in more subtle ways during the post-colonial era, has remained fundamentally unchanged. The present-day upsurge in the Muslim world is an expression of the Muslim peoples' repugnance to the politico-economic systems imposed upon them either directly under foreign rule or through its continuing influence via the indigenous westernizing élite, who stand mostly alienated from their own people and traditions and whose interests somehow converge with the interests of the dominant élite of the West.

Islamic resurgence symbolises the failure of the major Western models – Secular Democracy, Territorial or Linguistic Nationalism, Individualistic Capitalism and Totalitarian Socialism, to mention only the leading few – to take root in Muslim society and capture the imagination of the Muslim people. That is why all efforts to introduce a secular system in the Muslim lands have taken place under the protective umbrella of despotic rule. At the present moment the Muslim people are striving to reassert themselves by attempting to throw off their shoulders the yoke of various models of Westernisation or more correctly "West-domination", and also to get rid of their indigenous perpetrators. "Islamic revolution", symbolizing a holistic move towards a new civilization, is the target of the *Ummah's* tryst with destiny, whether it be Iran, Sudan, Pakistan, Turkey or elsewhere. The emergence of an Islamic republic in Iran, in spite of its teething problems and the external threats to its existence, is a product as well as a pace-setter of this historic trend.

Islamic resurgence must not simply be treated as an angry

outburst against the West as such. It does represent a rebellion against imposed Western models, political, economic and cultural, but more fundamentally it represents the Muslim people's search for a New Order which ensures justice to human beings in all aspects of life and seeks the ideological fulfilment of the *Ummah*. This quest for their destiny has made them more conscious of their ideological and historical identity and has brought them back to their original source – Islam. They are today grappling with the onerous task of rediscovering Islam's relevance to their present-day problems and of formulating its answers to the challenges of the modern age. In spite of all the tensions and travails which characterise the contemporary Muslim scene, the soul of the *Ummah* is engaged in producing a creative response to a multi-faced challenge. The contemporary Muslim is groping to perform the uphill task of establishing a New Social Order based on the ideals and values of Islam and capable of leading Muslims through the rough waters of the modern age. The revivalist upsurge is not confined to political activism or cultural regeneration. At a more deeper level there is a new awakening of Muslim thought and revivification of the entire Muslim ethos.

The emerging discipline of Islamic economics is one tiny but radiant element in this creative enterprise. Muslim scholars, particularly the "*Ulamā*" and the jurists, have during the last few decades produced a wealth of literature on different aspects of the economic and social teachings of Islam. The thought and vision of these pioneers have illuminated the horizon; the rays of light radiating from them have awakened the Muslim economists from their intellectual slumber, deepened by the sedentary effects of uncritical acceptance of all that came from the West in the name of Economics. These scholars presented Islam as a complete code of life and articulated a new approach to contemporary thought and ideologies. The works of Jamāluddīn Afghānī (Iran and Afghanistan), 'Allāma Muhammad Iqbal (Pakistan and India), Mawlānā Sayyid Abul A'lā Mawdūdī (Pakistan and India), Hasan al-Bannā Shāhid (Egypt), Sayyid Qutb Shāhid (Egypt), Imam Baqir al-Sadr Shāhid (Iraq), Mālik bin Nabī (Algeria), Dr. Ali Shari'atī Shāhid (Iran), among others, constitute the real source of this new intellectual and ideological awakening. They have piloted Muslim thinking to a new threshold. A brighter and more challenging world has now been opened up before the Muslim intellectuals.

The path is now being pursued by Muslim social scientists and policy-makers in their respective areas of interest and specialisation. The founding fathers broke the hegemony of Western thought on the Muslim mind and liberated it to discover its own course of development. They were not professional economists, yet they proved catalysts in challenging the conventional wisdom and in pointing to a new approach. The Muslim economists are now trying to develop, with professional rigour, a new discipline that could on the one hand spell out an Islamic critique of modern economics and economies and on the other undertake a reformulation of economic theory and policy in the light of Islamic values and principles and the thought and experience of mankind. We are passing through a period of creative transition, moving from a simple exposé on "Economic Teachings of Islam" to an articulation of what can technically be described as "Islamic Economics".

It may be of some interest to recollect that in our own times "economics of socialism" has passed through somewhat similar phases. Marx, Engels, and Lenin developed their critique of capitalism and gave an exposition of the philosophy of socialism. They had little to offer on what can be described as economics of socialism. The discipline was developed both at theoretical and applied levels during the post-Russian Revolution period. Perhaps the Muslim economists have begun to do to the evolution of Islamic economics what N. Bukharin, E. Preobrazhenski, V. Nemchinov, V. V. Novozhilov, L. V. Kantorovich and S. Strumilin (of the USSR), M. H. Dobb and H. D. Dickinson (UK), O. Lange and M. Kalecki (Poland), J. Kornai and T. Liptak (Hungary) and a host of others have done to the evolution of the economics of socialism!

It is in this context that the present work of Professor Syed Nawab Haider Naqvi, *Economics and Ethics: An Islamic Synthesis*, is of special interest.

Professor Naqvi is a leading Pakistani economist and has a wide experience of research, teaching and policy-formulation and appraisal. As director of the Pakistan Institute of Development Economics, he may rightly be described as the doyen of Pakistani economists. His "conversion" to Islamic economics over the last few years, has immensely strengthened the team of Muslim economists engaged in promoting new thinking and research in the nascent field of Islamic economics. He has already produced some valuable papers on certain aspects of Islamic economics and his present

work, I have no doubt, is going to be recognised as a major contribution in this field. It represents a happy and creative blend of two traditions in economics, Islamic and modern. The author has made a unique effort by using his masterly grasp of contemporary economics as a womb, for the operation of the creative process of reproduction, fecundated by the ethical axioms which represent to him the substance of the Islamic approach to economics and, nurtured by a strong moral commitment to see that man is enabled to live again in a just social order, ensuring simultaneously freedom and social justice, and not one at the cost of the other.

Professor Naqvi has developed a systematic approach to the study of Islamic economics. The alleged independence of economics from ethics has no place in his system. He has convincingly demonstrated that in the Islamic perspective ethics set the tone for economics, with the result that the rules of economic behaviour are derived from the ethical norms of Islam. This spells out a new matrix for individual and social behaviour along with clear and realisable guidelines for economic policy. Resort to this approach does not end up in a wonder-world of unreality as some of the critics of a moral approach to economics would like us to believe. In fact, this new approach to economics would lead towards the establishment of a higher and a different form of equilibrium, not just a technical state of harmony between factors and forces, but a real harmony ensuring justice and equity to all participants on the economic scene. That ethics leads the way is a fundamental principle of Islam and is acknowledged by all writers on the subject. The uniqueness of Professor Naqvi's treatise lies in developing a systematic analytical framework containing most of the essential ethical values of Islam, that could act as a basis for logical deduction of guidelines for economic policy. He has adopted an axiological approach, starting with ethical philosophy via mathematical logic to Islamic economics. The chief merit of this approach lies in transforming the rich and varied galaxy of the ethico-economic teachings of Islam into a condensed set of axioms from which the professional economist can deduce policy-relevant conclusions. This renders the Islamic teachings into a form with which the social scientist is familiar and opens the possibilities of the application of a methodology that has been tried in the discipline. It has the added merit of enhancing the communicability of the message of Islamic economics, as economists belonging to other traditions, including

the secular economics of the West, are familiar with this methodology. It would therefore be easier for them to understand the principles and the consequences of Islamic economics in this framework, as against the approach of distilling for themselves the essentials of Islamic economics by looking into the whole corpus of Islamic injunctions. I have no doubt that careful application of the axiological approach has the potential of providing the Muslim and non-Muslim economists with a common language for communication and dialogue. It will also enable the Muslim economists to develop a more systematized approach to the application of Islamic injunctions to problems of economics.

Professor Naqvi's contribution is not confined to elaborating a new methodology for Islamic economics and outlining a new matrix for the operation of economic forces. He has tried to develop a complete system, with its own assumptions, goals and objectives, rules of the game, institutional framework and instruments of policy. He has shown that the system is unique and that it has a way of its own in meeting the economic problems of man. He has eloquently demonstrated that the system is consistent, horizontally as well as vertically and that each part of it is inescapably related to the rest. As such it cannot admit of a strategy of pick and choose. It stands for a total transformation of the economic life to suit the new value-system, which it aims at actualizing. He has forcefully spelled out the implications of the concepts of Equilibrium (with a capital E), of Trusteeship and of Constrained Freedom (i.e. individual freedom in the context of social responsibility). His formulation of Islamic economics is not only logically sound, it is also rich with new insights, articulating before the economist the vision of a new man, committed to ideals higher than his personal interest, and of a society engaged in reordering its life and institutions towards a higher equilibrium based on justice and equity. I have every reason to believe that Professor Naqvi's book will be a seminal contribution to the future development of Islamic economics.

While welcoming *Economics and Ethics* as a pioneering work, I would pleasantly join Professor Naqvi in his frank and honest acknowledgement that the answers he has tried to offer need not be "the only answers possible". His methodology as well as his inferences, valuable as they are, represent efforts by one disturbed soul to find new answers to old questions, by drawing upon a different source of inspiration: Islam.

The ethical values that go to make up the set of axioms in the model of Islamic economics developed by Professor Naqvi would be accepted by most Muslim thinkers as essential to the Islamic system, although some may have certain reservations in accepting them as necessarily sufficient. *Tawhīd* (Unity) contains within it and leads to the concepts of *Risālah* (Prophethood), *Hidāyah* (Guidance) and *Akhirah* (Accountability) but some would prefer a definite place for them in the system, maybe as a cluster of values that go to make up the first plank of the axiom set. Each of these concepts has its own implications for the economic system, as well as certain modifying influences on the implications of one another. Similarly the concept of Freedom may also be formulated by others with a shade of difference. Human freedom as well as human responsibility are aspects of the concept of *Khilāfah* (vicegerency). Some of us would feel that while correcting the imbalance embedded in Western concepts of individualism and capitalism, the author's interpretation has tilted too much towards collectivism, with the result that the fine balance between the individual and the society has been somewhat disturbed. The delicate balance established by Islam through its concepts of *Fard 'alā al-'ain* (Individual responsibility that is non-transferable) and *Fard 'alā al-Kifāyah* (Collective responsibility dischargeable by even a few) deserve to be captured in the system. *Al-'Adl* (justice) is central to the Islamic system but it has to be supplemented by *al-Ihsān* (beneficence).

Moreover, the interregional implications of *al-'Adl* are as important as are the interpersonal and intertemporal ones. The question of the unity of the *Ummah*, its economic consolidation, and its non-dependence on the non-Muslim world are so integral to the system, by essential aspects of *Khilāfah*, that others may assign to this value a seat in the assembly of axioms. Professor Naqvi's emphasis on equitable distribution of income and wealth would be shared by all Muslim economists but it would be difficult for many of us to agree with the role he assigns to the institution of private property as such in generating this inequality. That unrestricted private property is *one* such factor no one would dispute; but to assume that near total abolition of private property is what Islam aims at for achieving social equity would be against the mainstream of Islamic thought, classical as well as modern. The Islamic concept of trusteeship does not exclude right of ownership, restricted by the use-limits laid down by the Qur'ān and *Sunnah*. There is very little evidence, logical or

canonical, to suggest that "collective ownership" is or has ever been the Islamic norm. More careful and rigorous differentiation between private ownership based on the concept of *amānah* (trusteeship) and the unrestricted private property and enterprise of capitalism as well as the collectivization of property in different brands of socialism deserves to be made. Similarly clear distinction between equity and equality, not to say of "absolute equality" (which unfortunately creeps into the text with reference to a highly controversial view of Abū Dharr), would have to be made by the Muslim economists. Islam's commitment to equity and a fair distribution of income and wealth ensure justice in society, without imposing any artificial equality over the unequals.

Professor Naqvi's views on *Ribā* are bound to provoke discussion and debate. Many of us, including the present writer, would regard his "first best" solution as one which would fail to fit into the Islamic system. As such many of us would lean heavily towards a new system of profit-sharing, which he regards as "second best"! However, we all agree that the abolition of *ribā* is destined to bring about such far-reaching structural changes in the organisation of the economy that any modification or adjustment with the capitalist system is out of the question.

I do not intend to dilate upon all those points in Professor Naqvi's thesis which may produce debate and discussion. Controversy is the breath of intellectual life and a stepping stone to progress. Professor Naqvi has produced a study which is thoughtful as well as thought-provoking. He is too great a mind to expect conformity or acquiescence even from his colleagues engaged in reflection and research in Islamic economics, not to say of the critics who do not subscribe to the idea of economics based on ethics. I am sure he is expecting lively debate on a number of issues he has raised and quite a few confrontations on many a position he has taken. I have always found him pungent and stimulating in a discussion. It is a delight to join him in an argument, a pleasure even to disagree with him. I am sure *Economics and Ethics* is going to offer to many of us not only a lot of food for thought but also quite a few shocks and challenges. Its value lies in making us think and in stimulating us to respond creatively. The challenge has come from a sincere and incisive mind. I for one look forward to a fruitful discussion and a creative debate. I have no hesitation in congratulating Professor Naqvi for coming up with such original, penetrating and provocative ideas. In spite of our

differences, all of us are bound to feel a little better off after the intellectual feast the author has provided.

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1st January 1981
23rd Safar 1401

Preface

The Islamic perspective on life is one of certainty, social harmony and dynamism. All these characteristics flow from the original Islamic philosophy which seeks to integrate, rather than differentiate, the various aspects of man's life through its "universal" ethical axioms, namely Unity, Equilibrium, Free Will and Responsibility. These ethical axioms form the fulcrum of the Islamic system, around which all of man's life must revolve. In particular, man's economic activities must be subjected to a dominant moral purpose enshrined in these ethical axioms. That being the case, the Islamic view of economics reduces to a sub-set of its cosmic ethical vision of life processes in general.

The Islamic emphasis on Unity, acting as an integrative force, provides man with a perspective of certainty since guidance along the path of finding the truth comes from God, who is Truth Himself. Furthermore, Unity makes it "natural" for man's economic behaviours to coalesce and reinforce each other. Equilibrium (i.e. *al-'Adl*), as the cohesive force in the Universe, dictates a middle-of-the-road philosophy leading man on to the "straight path" of social harmony, and enjoining him to avoid all extremes. Human freedom gets a new definition within the framework of the Islamic philosophy where the individual, though providentially endowed with Free Will, is never allowed to assume Promethean irreverence. Nor are *all* his preferences an infallible guide to social action. In particular, individual freedom that constitutes a negation of Unity or Equilibrium is not recognized in Islam.

Man must voluntarily curtail his own freedom in order to maximize collective freedom. This can best be done by increasing his social consciousness. This is the Responsibility axiom, which is both a restraining and a liberating force. It restrains (or rather constrains) human freedom by making man responsible not only for what he does but also for what goes on around him. At the same time, man has been asked (indeed commanded) by God to break the chains of

tradition. In forbidding him to be backward-looking or static, Islam is neither hidebound nor tradition-bound. Hence, there is no option left for him but to be forward-looking. Thus, contrary to what is often asserted about the static nature of the Islamic outlook on life, the doctrines of Equilibrium and Responsibility build into the Islamic system an irrepressible dynamism, which refuses to tolerate the predominance of obscurantist forces, which tend to prevent social change.¹ Should a class of social exploiters attempt to disturb Equilibrium, it is the responsibility of all men to restore it. In the Islamic perspective, this struggle goes on between the just people and those who are unjust irrespective of the "class" to which they may belong.

The central thesis of this book is that, in the climate of Islamic philosophy, it is ethics that dominate economics and not the other way round. Hence, the Islamic system differs from all other economic systems by an "ethical factor". This difference is fundamental because ethics epitomize the common values of a society and determine the preference structures of the members of that society. The key to a thorough understanding of the originality of the Islamic economic system lies, therefore, in its ethical value system. However, the predominance of ethics in the "universe" of Islamic thought does not exclude the possibility that economic conditions may, in extreme cases, influence the ethical behaviour of human beings. In fact, the Holy Prophet (Blessings of Allah and peace be upon him) has been quoted as warning his followers against extreme, *involuntary* poverty because it can turn men away from God.² What Islam asserts is that ethics, independent of the economic conditions prevailing at any time or in any society, must guide human behaviour for the attainment of social bliss as well as spiritual salvation. At the philosophical plane, this axiological view is the exact

¹ The argument that the conditions prevailing in the Muslim countries belie such a claim is entirely irrelevant, to say the least. In fact, it is their unjust, oppressive and static social systems which have been the proximate cause of the Islamic resurgence in the Muslim countries.

² It should be clearly understood that this tradition does not relate to the poverty which is *voluntarily* adopted, involving a renunciation of worldly comforts. It is in this sense that another tradition of the Prophet (Blessings of Allah and peace be upon him) should be understood: "My poverty is my pride". This is a poverty that comes from within, from a deep realization that man is poor before God, since all belongs to Him. It is in this sense that Islam is referred to as a "cult of poverty", which gives it the qualities of "ardour, courage, tenacity and generosity". See Frithjof Schuon, *Islam and the Perennial Philosophy*. London: World of Islam Festival Publishing Co. Ltd. 1976. p. 30.

opposite of the Marxian position, according to which economics dominate ethics, not only at the limited behavioural plane but also as a general rule. Islam also negates the capitalistic mentality which glorifies, out of all proportion, materialistic grabbing as a key to worldly success. In sharp contrast, the Islamic approach to economic problems is all-comprehending: "social bliss" is defined to include both economic betterment and spiritual ascension as two elements of a unitary Islamic outlook on what constitutes human happiness.

The general approach of this book is not at all apologetic. It is the author's conviction, amply substantiated in this book, that the Islamic system "exists" in the sense that it is logically, socially and economically viable. It is neither capitalistic, nor socialistic, nor a carbon-copy of a modern welfare state. This is not to deny that there may be some superficial inter-system similarities with respect to their elements, which is inevitable since all socio-economic systems face the same social "reality" – the age-old problems of want, poverty, disease and economic deprivation – though from different angles. However, such similarities do not deprive any social system of its claim to originality.

The main inspiration of undertaking research in this area, which at first looked rather odd to one trained as a professional economist in the Western universities, like Yale and Princeton, came from the recent resurgence of Islam throughout the world, including the full-scale revolution in Iran. No silent watcher of the social storm raging with unrelenting ferocity throughout the Islamic World, I, as a social scientist, could not fail to be deeply impressed by this unique phenomenon in recent history. How could religion be the cause of a full-scale revolution? In particular, how could Islam, practised for so long by people who are backward, living precariously in static societies, become an exceedingly potent force for social change upsetting the applecart of the existing social order in one country after another? To understand the reasons for all this, a deeper analysis must be carried out of what it is that Islam stands for and of the contribution it can make to free men from want, poverty and moral degradation. Furthermore, as one who believes in international amity and goodwill, I have been distressed to note that the nature of the world-wide Islamization movement has been grossly misunderstood in the West. To most, this appears to have been a step backwards – the Islamic reassertion acting as a time-

machine carrying its helpless passengers back to the Middle Ages – and, therefore, negative in character; while for others it is just a manifestation of a “militant Islam”. Both these impressions are completely wrong.

A negative and reactionary idea can never account for a social revolution, which always derives its strength from some kind of idealism, symbolizing a firm intellectual commitment to something dynamic and positive and to something that holds out hope for a better and more just future for the socially weak and the economically backward. For all those who gladly faced death in the cause of the Islamic revolution, the basic thing has been the overwhelmingly powerful idiosyncrasy, forever beholden to the truth of Islam as the last message of God, which induced them to remould the environment into a vision which they considered to be exclusively their own: the all-consuming passion of the Muslims to regain the Islamic Ideal, which, they were convinced, could deliver them from their present predicament. Hence, the legitimacy of the Islamic resurgence, indeed revolution, must be judged not merely by the mundane test of its success but ultimately with reference to the ideal which inspired it. This book is a modest contribution in this direction. It spells out the essence of the Islamic Ideal to highlight what it is that the Islamic resurgence is all about. Working through the economic implications of the Islamic vision of social dynamics, it should become obvious to the reader that an Islamic system is not a step backwards in history, but a big leap forward to a better, freer and a morally more dignified future – a future in which the weak and the poor and the downtrodden will receive the most important position in accordance with the Qur’ānic commandment, quoted as the title verse of this book. I hope this intellectual effort will provide a common ground where both Muslim and sympathetic non-Muslim economists and social philosophers can meet and view the matter with scientific detachment. This book is an “essay in persuasion” to cultivate goodwill and understanding through an active intellectual interaction on one of the most vital issues of modern times.

My intellectual odyssey in search of a basic organizing principle to derive the basic elements of Islamic economics started with my two articles³ on the nature of the Islamic economic system. My third paper⁴ explored in detail the various aspects of the Islamic prohibition of interest. The present book accepts the general approach of these papers and then builds on them in much greater detail,

although in several important ways I have departed from some of my earlier perceptions of the subject. I have learned a lot by reading and talking about Islamic ethics. In this area, previously unfamiliar to me, I have benefited the most from the various writings of Frithjof Schuon,⁵ Seyyed Hossein Nasr,⁶ Syed Qutb,⁷ Muhammad Iqbal⁸ and Syed Ameer Ali.⁹ In particular, the inspiration to include Equilibrium and Free Will in the axioms set came like a flash as I read through Schuon’s beautiful book, *Understanding Islam*. My understanding of the social significance of Unity is due almost entirely to Syed Qutb’s path-breaking essay. The pioneering works of Muhammad Iqbal and Syed Ameer Ali supplied the remaining axiom of Responsibility.¹⁰ However, the idea of collecting these four basic ethical principles into a logically “complete” system of axioms, and of taking them as the point of departure for my explorations into the fundamentals of the Islamic economic system is entirely my own.

I am convinced that in the “axiomatic” approach, which is by no means unique in the mathematical sense of being the only one possible, I have found a powerful analytical tool to help reconstruct, in terms of modern scientific knowledge, the basic elements of an Islamic economic system. This approach has the great merit of acting as an “assimilation” principle: whatever is “relevant” in modern economics and what does not contradict the ethical tetrad of Islam – Unity, Equilibrium, Free Will and Responsibility – must be made use of in our efforts to evolve Islamic economics. By the same

³ (a) Syed Nawab Haider Naqvi. “Ethical Foundations of Islamic Economics.” *Islamic Studies* (The Journal of the Islamic Research Institute, Islamabad, Pakistan). Summer 1978.

(b) Syed Nawab Haider Naqvi. “Islamic Economic System: Fundamental Issues.” *Islamic Studies* (The Journal of the Islamic Research Institute, Islamabad, Pakistan). Winter 1977.

⁴ Syed Nawab Haider Naqvi. “Interest Rate and Intertemporal Allocative Efficiency in an Islamic Economy.” Paper presented at the Seminar on Monetary and Fiscal Economics of Islam, held at Makka, October 1978.

⁵ (a) Frithjof Schuon. *Islam and the Perennial Philosophy*. London: World of Islam Festival Publishing Co. Ltd. 1966.

(b) Frithjof Schuon. *Understanding Islam*. London: George Allen and Unwin. 1963.

⁶ Seyyed Hossein Nasr. *Ideals and Realities of Islam*. London: George Allen and Unwin. 1966.

⁷ Syed Qutb. “An Islamic Approach to Social Justice.” In Khurshid Ahmad (Ed.), *Islam: Its Meaning and Message*. London: Islamic Council of Europe. 1976.

⁸ Muhammad Iqbal. *The Reconstruction of Religious Thought in Islam*. Lahore: Sheikh Muhammad Ashraf. 1960 (Reprint).

⁹ Syed Ameer Ali. *The Spirit of Islam*. London: Christophers. 1961 (Reprint).

¹⁰ It should be noted that Muhammad Iqbal also has spoken forcefully of the crucial importance of the concepts of Unity and human freedom. See [8] above.

machine carrying its helpless passengers back to the Middle Ages – and, therefore, negative in character; while for others it is just a manifestation of a “militant Islam”. Both these impressions are completely wrong.

A negative and reactionary idea can never account for a social revolution, which always derives its strength from some kind of idealism, symbolizing a firm intellectual commitment to something dynamic and positive and to something that holds out hope for a better and more just future for the socially weak and the economically backward. For all those who gladly faced death in the cause of the Islamic revolution, the basic thing has been the overwhelmingly powerful idiosyncrasy, forever beholden to the truth of Islam as the last message of God, which induced them to remould the environment into a vision which they considered to be exclusively their own: the all-consuming passion of the Muslims to regain the Islamic Ideal, which, they were convinced, could deliver them from their present predicament. Hence, the legitimacy of the Islamic resurgence, indeed revolution, must be judged not merely by the mundane test of its success but ultimately with reference to the ideal which inspired it. This book is a modest contribution in this direction. It spells out the essence of the Islamic Ideal to highlight what it is that the Islamic resurgence is all about. Working through the economic implications of the Islamic vision of social dynamics, it should become obvious to the reader that an Islamic system is not a step backwards in history, but a big leap forward to a better, freer and a morally more dignified future – a future in which the weak and the poor and the downtrodden will receive the most important position in accordance with the Qur’ānic commandment, quoted as the title verse of this book. I hope this intellectual effort will provide a common ground where both Muslim and sympathetic non-Muslim economists and social philosophers can meet and view the matter with scientific detachment. This book is an “essay in persuasion” to cultivate goodwill and understanding through an active intellectual interaction on one of the most vital issues of modern times.

My intellectual odyssey in search of a basic organizing principle to derive the basic elements of Islamic economics started with my two articles³ on the nature of the Islamic economic system. My third paper⁴ explored in detail the various aspects of the Islamic prohibition of interest. The present book accepts the general approach of these papers and then builds on them in much greater detail,

although in several important ways I have departed from some of my earlier perceptions of the subject. I have learned a lot by reading and talking about Islamic ethics. In this area, previously unfamiliar to me, I have benefited the most from the various writings of Frithjof Schuon,⁵ Seyyed Hossein Nasr,⁶ Syed Qutb,⁷ Muhammad Iqbal⁸ and Syed Ameer Ali.⁹ In particular, the inspiration to include Equilibrium and Free Will in the axioms set came like a flash as I read through Schuon’s beautiful book, *Understanding Islam*. My understanding of the social significance of Unity is due almost entirely to Syed Qutb’s path-breaking essay. The pioneering works of Muhammad Iqbal and Syed Ameer Ali supplied the remaining axiom of Responsibility.¹⁰ However, the idea of collecting these four basic ethical principles into a logically “complete” system of axioms, and of taking them as the point of departure for my explorations into the fundamentals of the Islamic economic system is entirely my own.

I am convinced that in the “axiomatic” approach, which is by no means unique in the mathematical sense of being the only one possible, I have found a powerful analytical tool to help reconstruct, in terms of modern scientific knowledge, the basic elements of an Islamic economic system. This approach has the great merit of acting as an “assimilation” principle: whatever is “relevant” in modern economics and what does not contradict the ethical tetrad of Islam – Unity, Equilibrium, Free Will and Responsibility – must be made use of in our efforts to evolve Islamic economics. By the same

³(a) Syed Nawab Haider Naqvi. “Ethical Foundations of Islamic Economics.” *Islamic Studies* (The Journal of the Islamic Research Institute, Islamabad, Pakistan). Summer 1978.

(b) Syed Nawab Haider Naqvi. “Islamic Economic System: Fundamental Issues.” *Islamic Studies* (The Journal of the Islamic Research Institute, Islamabad, Pakistan). Winter 1977.

⁴Syed Nawab Haider Naqvi. “Interest Rate and Intertemporal Allocative Efficiency in an Islamic Economy.” Paper presented at the Seminar on Monetary and Fiscal Economics of Islam, held at Makka, October 1978.

⁵(a) Frithjof Schuon. *Islam and the Perennial Philosophy*. London: World of Islam Festival Publishing Co. Ltd. 1966.

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⁶Seyyed Hossein Nasr. *Ideals and Realities of Islam*. London: George Allen and Unwin. 1966.

⁷Syed Qutb. “An Islamic Approach to Social Justice.” In Khurshid Ahmad (Ed.), *Islam: Its Meaning and Message*. London: Islamic Council of Europe. 1976.

⁸Muhammad Iqbal. *The Reconstruction of Religious Thought in Islam*. Lahore: Sheikh Muhammad Ashraf. 1960 (Reprint).

⁹Syed Ameer Ali. *The Spirit of Islam*. London: Christophers. 1961 (Reprint).

¹⁰It should be noted that Muhammad Iqbal also has spoken forcefully of the crucial importance of the concepts of Unity and human freedom. See [8] above.

token, this approach does not permit an indiscriminate borrowing from "alien" (i.e. non-Islamic) economic systems. It is hoped that this way of looking at the subject matter — i.e. the axiomatic approach — will be widely adopted by researchers in the unexplored and challenging area of Islamic economics. For it strikes the middle course — which is what Islam advises us to do — between the ultra-conservative view, which scornfully rejects all modern knowledge on the unacceptable argument that everything useful and valid on Islamic economics has already been said, and the so-called liberal view, which accepts everything modern as Islamic. The analytical scheme followed in this book has permitted me to evolve a "balanced", multidisciplinary approach in which mathematical logic, ethics and economics reinforce each other to highlight the basic characteristics of Islamic economics — an approach that is symbolic of the unitary Islamic philosophy according to which knowledge is a homogeneous whole. It is a modest attempt, but worth noting.

I am deeply aware of my limited knowledge of the vast subject of Islamic studies. Those who are more knowledgeable about the Holy Qur'ān and the *Sunnah*, the primary sources of everything that is Islamic, should be able to get deeper results through this approach than it has been possible for me to derive. It is for this reason that I have relied very heavily, particularly in formulating views on Islamic ethics, on the works of other scholars who have spent their life-time on researches into the various aspects of Islamic philosophy. However, my main source of inspiration and information on Islam is where all truth lies: the Holy Qur'ān. I admit that it is not without a certain apprehension about my ability to interpret them that I have used the Qur'ānic verses extensively to establish the basic propositions of this book — in accordance with the Qur'ānic commandment: "Whoso judgeth not by that what Allah hath revealed; such are evil-livers" (5:47). There may be honest errors of interpretation, but I have never tried to stretch the meaning of any of the verses to suit my point of view, for that, according to Islam, would have been a blasphemy. It has been my good fortune that the thrust of my argument, which is perfectly general, happens to be in the direction indicated by the Holy Qur'ān.

In exploring the difficult area of Islamic studies, I have held fruitful discussions with many of my close friends. I am deeply indebted to Khurshid Ahmad for his constant encouragement. His

numerous writings on Islamic economics have been of great help. I must also mention Rafiq Ahmad, Mian M. Nazeer and Ziauddin Ahmed who have been patient and understanding listeners to many of the basic ideas expounded in this book. Thanks are due to A. R. Kemal, Anas Zarqa, Asghar Qadir, Ijaz Gilani and Ziaul Haq for a useful exchange of ideas. Needless to say none of these scholars shares blame for any of the shortcomings of the analysis presented in this book. I am especially indebted to Mr. Syed Hamid Hasan Naqavi, who painstakingly went through the typescript and gave invaluable editorial assistance. I also wish to record my appreciation of the excellent typing work done by my Secretary, Muhammad Aslam.

My greatest debt of gratitude is to my deceased parents, my uncle and aunt, and to my younger sister, Nasim Zehra, who helped me in acquiring the sympathetic attitudinal make-up that has been an essential building-block in my entire approach to social problems. Their deeply-felt compassion for the poor and the weak convinced me very early in my life that not much useful can be achieved by a social scientist without intellectual honesty and a broad social sympathy. Many thanks to my wife, Saeeda Nawab, without whose understanding and co-operation I could not have found the time or the energy to complete this work. Not only that. I have discussed many of my ideas with her on substantive matters as well, always coming away with the feeling that, if given equal opportunities for intellectual endeavours, women are in no way inferior to men in the attainment of intellectual excellence. I very much hope that our four daughters, to whom this book is dedicated, will prove, through intellectual accomplishments, this conviction of their ever-optimistic father.

Islamabad
November, 1980.

Syed Nawab Haider Naqvi

Introduction

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"Say: Each one doth according to his rule of conduct, and thy Lord is best aware of him whose way is right"

The Holy Qur'ân (17:84)

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The dichotomy of man's life into mundane pursuits and his spiritual aspirations has contributed immensely to the schizophrenic confusion prevailing in the modern world. Dualistic cultures, riddled with inherent contradictions, have sprung up, spreading social tensions. The Islamic solution is to destroy this artificial schism by providing a unitary philosophy of life, according to which no "moral vacuum" can exist on the plane of social existence. Accordingly, in the context of the immaculate Islamic vision of Unity, the distinction between the secular and the spiritual becomes both meaningless and inconsequential. The Holy Qur'an has advised all mankind to seek God's mercy in both: "Our Lord! Give unto us in the world that which is good and in the Hereafter that which is good..." (2:201).¹

This philosophy is as enlightening as it is exciting, making a direct appeal not only to emotions but also to reason. Man, by virtue of his theomorphic character, occupies a unique place in this philosophy, which guarantees him freedom and imposes the concomitant social responsibility. True, a certain authoritarian zeal permeates all ethically-oriented social orderings, yet the attitudinal framework that Islam provides is such that intellect is strengthened at the same time.

This is because Islam's attitude towards life processes is based on the quality of *al-'Adl* (i.e. Equilibrium). A Divine serenity, like the light which is neither blinding nor too dim, permeates the Islamic vision of human societies. The "straight path" of Islam is balanced on a knife-edge, any deviation from which will plunge mankind into the abyss of eternal condemnation. However, since human society is liable to deviate, as happens so frequently, from the "straight path", it is obligatory on man, individually and collectively, to return to this path. Hence, Equilibrium is also a normative requirement that

¹ Throughout this book the English rendering of the Qur'anic verses is from Marmaduke Pickthall [9]. The first number in the parenthesis refers to the *Sūrah* (chapter) in the Holy Qur'an, while the second denotes the *Ayah* (verse) in that chapter.

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must be met. Within the Islamic perspective, the obligation to fulfil this requirement is enforced by making man directly responsible not only for what he does himself but also for his immediate environment. Never alienated from the universe around him, man makes his own destiny. This is a difficult task, because a thousand temptations lie in ambush to turn him away from the path of salvation. Accordingly, man has been advised to constantly pray to Allah: "Show us the straight path, the path of those whom Thou has favoured; Not (the path) of those who earn Thine anger nor of those who go astray" (1:5-7).

Islam's prefiguring vision is an arabesque wherein are blended the religious, economic and social dimensions, providentially equilibrated to form a unity. Within the ethical limits prescribed by Islam, even the search for economic well-being gets sanctified. The way to Heaven passes through the Earth; in fact, the Holy Qur'an condemns misplaced self-denial. "But seek the abode of the Hereafter in that which Allah hath given thee and neglect not thy portion of the world" (28:77). As a result, ethics and economics become integrated, vertically and horizontally, to form a vital equation within a homogeneous Islamic system, which tolerates neither "kinks" nor any discontinuity.²

This Divine Synthesis between man's desire to cling to material possessions and his equally strong longing for spiritual ascension guarantees the "completeness" of the Islamic system, informing mundane pursuits with a sense of the sacred. However, it is important to bear in mind that, while it is true that the Islamic way of life forms a self-sufficient orbit of social, economic and moral values, it is by no means insular. It is not a limiting concept which pre-empts innovative ideas but a starting point opening up new horizons for breath-taking initiatives. It is this fact which ensures the dynamism of the Islamic economic system. In fact, "Islam was given providentially the power to synthesize, to integrate and absorb what was in conformity with its perspective from previous civilizations" [6,

² Even at the intellectual plane, the need of some kind of synthesis becomes compelling, once human behaviour is seen in relation to religion. This is because religion looks at man as a homogeneous whole, and the Divine Message sees reality in totality. Islam's originality lies in combining within one all-comprehending Vision the temporal and the spiritual aspects of man's life. As Iqbal has profoundly remarked, "It is the mysterious touch of the ideal that animates and sustains the real, and through it alone we can discover and affirm the ideal. With Islam the ideal and the real are not two opposing forces which cannot be reconciled" [4, p. 9].

p. 36]. As a living religion, Islam cannot fail to absorb from its surroundings what conforms to its native genius. To maintain that everything useful about Islamic economics has already been said will frustrate all potentialities of intellectual advancement in this area of knowledge. History often repeats itself, but seldom in the realm of ideas. Or else, the life of an intellectual would not have been so difficult or, shall we say, interesting.

The world has come a long way since the Middle Ages. It has become much more complicated than it ever was; and easy solutions, which sufficed in those halcyon days of ascetic simplicity have become totally inadequate in the modern world of sensuous affluence. Even worse, we do not have anywhere, in full operation, a model Islamic economic system which could be "simulated" and generalized to form the basis of Islamic Economics. True, Muslim philosophers, like Fārābī (d. 950 AD), Ṭūsī (d. 1274 AD) and Ibn Khaldūn (d. 1375 AD), wrote extensively on economics,³ yet they all belonged to a different socio-economic milieu. The brilliance of these scholars, like that of the stars of yore, which once illuminated the intellectual firmament, has dimmed gradually with the passage of time. Their profound writings still attract our admiration, but offer little help or guidance in facing with confidence the complexities of modern life.

The task of the modern Muslim economist is much more difficult than to relive the past in a mechanical fashion. It is to rediscover the fundamental verities of Islam in the vastly complicated world of today, with a view to improving upon what already exists: integrating what relevant knowledge is already available and transmuting it into a new frame of thought. In fact, this is how originality in the realm of ideas is defined in the Islamic perspective. Human knowledge, irrespective of its source, is the common heritage of all mankind. No purpose will be served — indeed, great harm will be done — if the existing economic wisdom, which has been generated through the long process of active intellectual interaction, is ignored in the formulation of our views on Islamic economics. After all, Muslim philosophers did study Pythagoras, Plato and Aristotle to propound the Islamic point of view on science and metaphysics in a language which even non-Muslim philosophers and scientists could

³ For a valuable discussion of the origins of economic thought among the early Muslims, see Rafiq Ahmad [1].

understand. The present essay seeks to continue that noble tradition.⁴

However, the translation of "alien" precepts – i.e. those alien to the Islamic economic system – to the plane of Islamic economics cannot be carried out in a mechanical fashion, certainly not by an indiscriminate syncretism. What essentially runs counter to basic Islamic ethical values cannot be accepted in the Islamic fold. Hence, the first step in the direction of evolving Islamic economics is to recognize and understand clearly what these fundamental ethical values are in order to discover the touchstone by reference to which one could establish the Islamic (or un-Islamic) nature of given economic principles. The next step along this difficult road is to turn these ethical values into "operational" axioms. Once such a logical system has been set up, the essentials of Islamic economics can be deduced in a finite number of steps.

This analytical procedure amounts to delineating Islamic economics by reference to the "first principles", which, in the climate of an Islamic system, are all ethical. There is nothing unscientific about this procedure of the tracking down of economic principles to ethical precepts since, in the last analysis, all scientific systems are based on a system of commonly accepted values – which is what ethics are, broadly defined. At any rate, in so far as ethical principles are required to effect a meaningful rank ordering of social preferences, no economic system worth the name can ignore them. It is a difficult undertaking; but then this is the only way of doing the job scientifically. No royal road exists to knowledge. However, it is important to bear in mind that the basic propositions of Islamic economics can be valid only within the framework of an Islamic system, of which ethics form a dominant component. This follows logically because the basic propositions of every "complete" logical construct, not only of economics, are formally correct only within the matrix of such a system.⁵ However, this fact does not detract from the "universality" of such a system; it only points to the essen-

⁴ Iqbal had taken cognizance of the need to reconstruct the Muslim religious philosophical tradition of Islam and the more recent developments in the various domains of human knowledge: "... our duty is carefully to watch the progress of human thought, and to maintain an independent critical attitude towards it" [4, p. vi of the Preface].

⁵ For instance, even a "universal" truth that "three angles of a triangle are equal to two right angles" is valid only within the Euclidean geometrical framework; it is false in the context of, say, spherical geometry.

tial relativity of all human knowledge – that pertaining to Islamic economics being no exception to this universal rule.⁶

Plan of Work

The subject-matter of this book has been divided into ten chapters, along with a Preface and an Introduction. The level of exposition throughout the book, except perhaps in two chapters, is such as to make it accessible both to economists and to general readers of the literature of Islamic economics. In terms of its scope, the book is comprehensive but not exhaustive. In fact, each chapter can easily be enlarged into a monograph. My aim in these pages has been to assemble the building blocks of an Islamic economic system that is distinctive but never unreasonable or isolationist. The first chapter reviews briefly the fundamental principles of scientific enquiry, emphasizing that theory must, above all, be "simple", i.e. it should consist of a *minimum* number of axioms to remain operationally manageable; and it should be free from inconsistency. This is the basic message of what Einstein called, in the context of theoretical Physics, the principle of "Optimal Methodological Simplicity". Furthermore, as Popper emphasized, the axiom system must possess "predictive" power, i.e. it must be "general" in the sense of its ability to explain the diverse phenomena with reference to a set of general organizing principles.

The second chapter attempts to set up a logically consistent Islamic axiom system. This is a fundamental step for the argument of the rest of the book because any logical "statement" presumes a set of distinctive axioms on which it depends for its validity. Once that step has been taken, the researcher can no longer appeal to anything outside of a specific axiomatic system to verify the truth or the falsity of statements made within the overall framework of specific logical systems. It is important to note that the fundamental axioms themselves are derived not through any logical process, but through observations or by positing a value judgement about their universality. We have based the Islamic axiom system – consisting of exactly four elements, namely, Unity, Equilibrium, Free Will and Responsibility – on the observations and value judgements con-

⁶ In the tradition of Western economics, Karl Marx was the first to point out in *Das Kapital* the specificity of economic laws to particular economic regimes. Furthermore, according to Marx, no economic regime could be understood without reference to the social structure in which it was embedded. See Raymond Aron [3, Chapter 3].

tained in the Holy Qur'ān and the *Sunnah*, both of which have a supreme claim to universality, at least in the eyes of the Muslims.

The third chapter, building on these four ethical axioms, identifies the broad contours of an Islamic economic system. The analysis shows that once ethical considerations are made binding, economic behaviour undergoes a profound transformation. A new concept of the "allowability constraint" has been introduced to clarify what an integration of economics with ethics implies for economic policy-making. To bring out the Islamic point of view in sharper focus, it has been contrasted in the fourth chapter with the three existing economic systems – Capitalism, Socialism and the Welfare State. This analysis, conducted within the axiomatic framework laid out in the second chapter, shows clearly that no existing economic system can completely satisfy all the Islamic ethical axioms. Hence the need of a distinct Islamic economic system which does satisfy them. It may be noted that there is nothing tautological about this line of argument, since it asserts a perfectly legitimate point that both the axioms and their consequences form a distinctive logical system, so that the truth of the latter cannot be verified without reference to the former. This is another way of saying that the basic economic propositions of an Islamic economic system are true only within that system, pointing to their essentially "relative" character.

Having established, in terms of the first principles, that an Islamic economic system "exists", the next logical step is to investigate the mechanics of an Islamic economy in terms of its choice of the policy instruments required to achieve certain policy objectives. This is a complex issue, the discussion of which is spread over Chapters 5 to 8. The fifth chapter lays down the fundamental policy objectives of such a system. Once again the axiomatic system has been used as a basis for making an optimal choice of policy objectives with respect to their consistency with the Islamic ideal. These turn out to be social justice, an optimal rate of economic growth, universal education and maximum (*not* necessarily "full") employment.

The sixth, seventh and eighth chapters outline economic policies most suitable for an Islamic society, and which can best attain the basic economic objectives *without contravening any of the axioms stated*. The discussion in these chapters highlights the fundamental point that, in the ethically-charged environment of an Islamic system, not only the ends but also the means, or policy instruments, must be Islamically legitimate, i.e. "first-best" from an Islamic point

of view. However, the validity of these policy instruments is contingent upon the establishment of a fully-fledged economic system. This is not a question-begging observation, but points to the extreme complexities of the "transition period" – the transition from the present un-Islamic economic systems to a complete Islamic economic system. During this period, depending upon the best strategy chosen, a "second-best" choice may have to be made with respect to the selection of policy instruments, given the "institutional" constraints and the limitations of human knowledge at a given point of time. However, these second-best choices will be in the nature of a *pis aller* to be gradually discarded as the Islamization process gathers momentum, expanding our knowledge about the alternative courses of action which Islam approves of.

This is the subject-matter of Chapter 9, which, along with the final chapter, brings together the foregoing analysis to form the basis of a sequential approach to Islamization. The general thrust of the argument in these chapters is that while the universal truth of Islam cannot be questioned, at least by Muslims, it will take time, effort and ingenuity to "make room" for it, and to accommodate it. The Divine Vision is immaculate and unfettered by space or time, and views reality as a homogeneous whole. However, man is essentially myopic and time-bound. He must approximate the Islamic Reality, without having to compromise it, in carefully graduated steps. Institutional constraints weigh heavily on the speed of change, slowing it down just enough to maintain the continuity of life processes. Social change should contribute to the continual advancement of human institutions. *It should not tear apart their organic unity*. The gravitational pull of "what is" makes it hard for man to opt out for "what ought to be". In the modern Muslim societies, which are by no means fully Islamic, the sacred and the profane – from an Islamic point of view, that is – have become mixed up, and it is not always possible to disentangle with ease one from the other. The intellectual odyssey of moving out of the shadows of ignorance into the sunlight of knowledge cannot be easy. Let there be no complacency about the extreme complexity of the task ahead. No emotional rhetorics can end the winter of our discontent and usher in an era that we have been looking for. Meaningful and honest gradualism should set the pace of our march towards the Islamic El Dorado. It will take hard work and patience, with the Divine assurance that "Allah is with the steadfast" (2:153).

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PART I

THE ANALYTICAL FRAMEWORK

"We shall show them Our portents on the horizons and within themselves
until it will be manifest unto them that it is the Truth"
The Holy Qur'an (41:53)

CHAPTER 1

General Considerations

Granted that in the Islamic perspective ethics dominate economics, the first step in the direction of identifying the basic characteristics of an Islamic economic system, which is distinct from the existing economic systems, is the search for a set of "general" ethical principles, which are unambiguously Islamic. This is what scientific enquiry requires us to do: namely, proceed from the general principles to the particular in order to ensure scientific "objectivity" as well as clarity of thought. It is only in this way that, instead of formulations relating to particular situations, certain general principles can be derived by reference to which the Islamic or un-Islamic character of any particular proposition can be clearly established. On the plane of social existence also, a set of "ground rules" of sufficient generality must be found to avoid *ad hocism* in human affairs which, in most cases, leads to anarchy and authoritarianism.¹

The quest for general principles implies a value judgement about the sources where we can find them. The Western social philosophers have generally discounted religion as such a source. The thesis presented in this book, which is fundamental to all that follows, is that Islamic religion, explicated through the Holy Qur'ān and the *Sunnah*, does constitute a reference point which can be used as a basis of the derivation of general principles of social behaviour. It offers to the world a unitary philosophy which is "internally" consistent and is capable of cutting through the web of the moral and intellectual confusion of our Age. It not only lays down a number of ethical objectives but also sets definite pointers as to the probable means of achieving them. The general requirement is that both the ends and the means must be Islamically legitimate. Even though the objectives and the means for achieving them are not always

¹ Hayek observed: "the aversion to general principles and the preference for proceeding from particular instance to particular instance leads us back to a system in which order is created by direct commands" [4, p. 1].

explicitly laid down, these can be deduced readily once we agree on a minimum set of ethical axioms, which adequately summarize Islam's ethical philosophy.

Characteristics of the Axiom System

A clear identification of an appropriate Islamic axiom system is one of the fundamental aims of the present study. However, such a system, to be viable and meaningful, must satisfy the following requirements:² (i) the axioms must be an "adequate" and a legitimate representation of Islam's ethical views; (ii) the set of axioms must be the "smallest" possible set; (iii) the elements of the set must be internally "consistent"; and (iv) the axiom system must have "predictive power". Each of these properties needs a brief explanation. The first property stipulates that the axioms must summarize accurately Islam's ethical stance. Furthermore, it implies that, of the infinite number of axioms existing side by side with the finite set stipulated, only those qualify to be in the set which are Islamically legitimate, i.e. these should be shown to follow from the Holy Qur'an and the *Sunnah*.³ This requirement guards against subjective arbitrariness in the choice of ethical axioms.⁴

The second requirement, that the set must contain the smallest number of elements, is the property of all mathematical axiom systems. It makes them manageable and meaningful. However, it should be noted that smallness is used in the sense of a logically irreducible minimum number; or, in the more graphic parlance of vector analysis, in the sense of a "spanning set".⁵ This property

² These general requirements must be satisfied by all logical axiom systems.

³ This is an application of Godel's Theorem in mathematics which stipulates that, given a finite set of assumptions, there exist other assumptions (infinite in number) which, or the negation of which, should be consistent with a particular theory.

⁴ True, there is always a subjective element in the choice of any ethical system, especially when it is made the basis of deductions about Islamic Economics. Indeed, this is true of all kinds of scientific elaborations. However, there is nothing arbitrary about this procedure since subjectivity here does not mean *personal* preferences of the author.

⁵ As a technical footnote, the "spanning set", also called the *basis*, is not "unique" (i.e. the only logically possible set). In fact, there can be an infinite number of bases in "Euclidean space". See Hadley [3, pp. 39-45]. This is particularly true of the "social space", where there is more "room" for such a different combination of axioms forming a basic set. This observation should make absolutely clear the point made at several places in this book that there may be other such "spanning sets". It is only that in terms of its explanatory power ours appears to be the best possible collection of axioms. Other authors may differ from our judgement and construct alternative axiom systems, by showing that theirs are better explanatory tools.

eliminates what is redundant and ensures that no two elements in the set are inconsistent with each other. It also makes the system "simple" which, as Einstein enunciated in his principle of "Optimal Methodological Simplicity", is an essential building-block of all logical systems. Otherwise, as an analytical tool, the system will be too unmanageable; indeed, useless. The whole point of the present exercise is to find a set of axioms which has the capacity to span (i.e. generate) the entire system – in the present case, the Islamic economic system.

The third requirement of consistency is absolutely basic to the validity of the entire system. A stricter requirement for checking on the consistency of mathematical axiom systems is to ensure that the axioms in the system are logically "independent" of each other. In a mathematical sense, this means that if one element of the axiom system is replaced by its negative, then no contradiction should be introduced into the system.⁶ However, this test cannot be meaningfully applied in social sciences, where the property of independence can be satisfied only in a very broad sense because of the highly interacting nature of the social phenomena. We would, therefore, use the consistency test in the more heuristic sense: the truth of one axiom should not belie that of another axiom in the set, and each of the axioms must point to a common "truth" about the system as a whole. Specifically, when the system is oriented towards the Islamic ethical value system, none of its elements should be pointing towards a value system contrary to Islam's.

The last property, requiring that the system must possess "predictive" power, simply indicates its ability to explain the maximum number of particular phenomena with reference to the general principles contained in the system. Indeed, the essence of scientific method is to discover a general theory which can unify particular theories of a discipline with respect to its central features, and integrate its diverse elements into a meaningful analytical framework [8, esp. Chapters 1 and 2]. The basic contention of this essay is that Islam's ethical system provides such a general theory in that it can explain the multifaceted economic behaviour in an Islamic society with reference to its essential unitary character. It is important to understand what this statement implies. At a deeper level, it

⁶ For a full discussion of the criterion of "independence" of the axiom system, see P.S. Novikov [5, Ch. 2].

highlights the "relative" character of Islamic economics: its basic propositions hold only within the radius of the Islamic ethical value system. In this sense, these propositions may not be "universally" valid, if the universe is defined to include the incompatible elements of the value systems of other religions as well. However, this is by no means a "defect" of the Islamic economic system; it is merely a statement of a general truth.

Before we turn in the next chapter to the main task of identifying an "operational" Islamic axiom system, it may be useful at this point to discuss briefly the legitimacy of using ethical axioms as a basis for economic formulations. Such a procedure, of going from ethics to economics, should cause no qualms in the scientist's conscience who always uses a pre-assigned value system as a reference point for scientific elaborations.⁷ Indeed, scientific behaviour is, in general, motivated by a goal and a set of values. This is all the more true of economic behaviour. There is a growing realization among economists that *wertfrei* (value-free) economics, such as Lionel Robbins once propagated, is a misnomer. At any given point of time, the maximization of social welfare requires the "superimposition" of a social welfare function to reflect the "best" rank ordering of social preferences. This cannot be done meaningfully without reference to the "universally" accepted ethical norms in a particular society. Furthermore, the very dynamics of social change require an explicit knowledge and understanding of preference structures, which in turn are determined by the ethical norms of the "sub-culture" the economic agents subscribe to.⁸ It may be interesting to recall the

⁷ It is interesting at this point to recall Raymond Aron's distinction between a value judgement and a value reference, where the latter serves as an organizing principle, i.e. a means of selecting and organizing a part of the reality to be studied. As opposed to the Kantian philosophy, the Newtonian or Einsteinian physics relates matter to values in constructing mathematical systems, using a deductive method [1, pp. 229-318]. The assertion made in this study, that ethics predominate over economic behaviour in an Islamic system, may be considered both a value judgement and a value reference. Indeed, it is more of the latter, since we have used Islamic ethical values as a reference point for deriving economic propositions relevant to an Islamic society.

⁸ This is so because ethics, broadly interpreted, are symptomatic of the generally accepted moral norms and propositions about how individuals rank order their preferences. See Kenneth Boulding [2, p. 123]. The point that the ethical code must be comprehensive to include both the social and the individual behaviours of men has also been noted by many social philosophers. For instance, Bertrand Russell maintains: "We must therefore admit two distinct elements in human excellence, one social, the other solitary. An ethic which takes account only of one, or only of the other, will be incomplete and unsatisfying" [7, p. 17].

Weberian thesis that the rise of capitalism in the West presupposed a universal acceptance in the West of Protestant ethics which legitimized unlimited accumulation of wealth and extolled thriftiness and worldly ascetism, even if it meant causing considerable social suffering. An important implication of this thesis, which appears to be highly plausible, is that the economic performance of a society cannot be separated from its moral philosophy, which since the dawn of civilization has proved to be a dominant force in shaping attitudinal reaction patterns in one society after another.⁹ In general, the implicit logic of the socio-economic behaviour of a people can be traced back to their metaphysical or religious conceptions. For instance, the economic behaviour of a Muslim is deeply influenced by his firm belief in the Day of Judgement and the life after death. A complete description of what constitutes rational behaviour in an Islamic economy must include such apparently irrelevant metaphysical considerations as well.

Adequacy of the Ethical Axiom System

One of the central theses of this book is that the Islamic ethical philosophy can be exactly summarized by four ethical axioms: Unity, Equilibrium, Free Will and Responsibility, which together form a "spanning set". The set is not necessarily unique in the sense of being the only one possible as a basis of valid generalizations about the Islamic economic system. The next chapter explains these axioms in detail. At this point, it is interesting to note that the Islamic ethical axiom system satisfies all the requirements of these logical constructs. It is simple as well as consistent and possesses great predictive power. That the system is simple in the sense of smallness should be obvious: it has exactly four elements. By the same token, it is also "manageable". However, the more fundamental question pertains to the demonstration that the set of axioms is the smallest possible — that it is in fact a spanning set. In other words, is it possible to drop one or more of the elements of the set as "dependent", i.e. "redundant" from a logical point of view? It may be argued, for instance, that Equilibrium is implied by Unity, and that Respon-

⁹ It is no wonder that many of the propositions found in Adam Smith's *Wealth of the Nations* can be traced back to his treatise on moral philosophy. See Chapter 4 of the present book for more details of the Weberian thesis.

sibility is a property of Free Will. Hence, the set of axioms may be contracted to contain only two elements, Unity and Free Will. Or, going even farther, since everything follows from Unity, the set should have only one element.

In fact, there are authors who have used only the concept of Unity to derive the basic principles of Islamic social justice.¹⁰ While at a metaphysical level this may be a valid procedure, it is not at all adequate either from a logical or from an "operational" point of view. Logically, Unity is "independent" of Equilibrium, since the vertical and horizontal dimensions cannot be arbitrarily collapsed into one without reducing the "dimension" of the Islamic space.¹¹ Furthermore, philosophically, Unity does not automatically make explicit the Divine quality of Equilibrium. As shown in the next chapter, the concept of Equilibrium must be introduced at the level of the Absolute to make clear the Islamic perspective according to which God is essentially *al-'Ādil* (i.e. the Just), and not just an arbitrary omnipotent overlord. On the plane of human existence, the need of an additional axiom, which takes care of its horizontal aspects, is essential to provide an adequate framework for analysing questions of social justice – a problem which cannot be satisfactorily tackled with reference to the Unity axiom alone.

As for the other two elements of the set – Free Will and Responsibility – it should once again be clear that the one does not automatically imply the other. Free will does not necessarily lead to a socio-economic framework which is unambiguously Islamic, unless ethical constraints contained in the Doctrine of Responsibility are *explicitly* introduced. Free Will can lead to a denial of Unity and also upset Nature's Equilibrium if man is not made responsible for what he does. It should, therefore, be clear that Responsibility introduces an additional dimension to the Islamic socio-ethical "space".

It also follows from this discussion that the set of Islamic ethical axioms is "consistent", in the broad sense defined earlier on, because the truth of one axiom does not belie the truth of the other axiom in the set. In fact, all the four axioms reinforce the basic Islamic ethical principle, which aims at producing an integrated, just and fruitful

¹⁰ See, for instance, the excellent work by Syed Qutb [6].

¹¹ It has been pointed out in the next chapter that while Unity forms the vertical dimension of Islam, Equilibrium constitutes its horizontal dimension.

socio-economic ordering to maximize material happiness without in any way depriving man of the possibilities of spiritual advancement. As pointed out above, this can't happen if Free Will reigns supreme, unfettered by Responsibility, or if the quality of Equilibrium were suppressed in an arbitrary manner.

As for the predictive power of the proposed axiom system, it suffices to note here that the system provides a set of necessary and sufficient conditions for a truly Islamic socio-economic ordering – i.e. not only does an Islamic ordering imply these axioms, but these axioms also imply a social rank ordering based on the teachings of Islam. The necessary part of this statement can be "proved" if it can be shown that the set of axioms is independent, a point heuristically demonstrated above. Its "sufficiency" also follows from the main thesis of this book that the set of axioms is a spanning set: i.e. all the basic principles of an Islamic economy can be derived from this axiom system.¹² The demonstration of this assertion is the central feature of the analysis presented in this book. It also highlights the essential relationship between Islamic ethics and Islamic economics, and, by implication, draws attention to the distinctively "humane" character of the latter, which forbids immoral, unethical economic behaviour *even if it is "rational" and profitable*. For instance, a Calvinist ethical philosophy, which permitted an unlimited accumulation of wealth during the Industrial Revolution of 1776, cannot (and *must* not) find an echo in an Islamic economic system since the Responsibility axiom will block it.

Summary

It should have become clear by now that an Islamic ethical axiom system, as an analytical tool to explore the nature of the Islamic system, is an adequate framework, which eliminates the possibility of any inconsistency arising between man's spiritual aspirations and his legitimate material pursuits. Spiritual bliss and material happiness come together in the Islamic unitary vision, which is

¹² Another way of looking at the matter is to convert the "if and only if" condition into two "if" parts. The above statement would then read; the axiom system implies an Islamic economic system; and the Islamic system implies these axioms. The truth of these assertions should be transparent if it is remembered that both the Islamic system and the ethical axiom system are based on the Qur'an and the *Sunnah* and must, therefore, imply each other.

perfectly equilibrated and balanced, ensuring man's innate freedom but simultaneously constraining the individual so as to maximize collective freedom and social happiness.

At a philosophical level, much of the utility of social science comes from the high degree of sensitivity of its practitioners to the problems of the real world. This awareness is reflected in the type of questions they ask. It is precisely the ability to pose the "right" type of questions that determines the *quality* of social science. However, in doing so, no social scientist worth his salt can ignore the basic values of the society he undertakes to study. Muslims all over the world are passing through a unique period in history which is making them look for their guidance to the Islamic value system that makes a claim to be "complete". Hence, it would be unscientific to study their economic behaviour in isolation from the context of the relevant ethical environment. Indeed, in the strict Weberian sense, economic behaviour in an Islamic society will transform into effective action only in so far as it is immediately dictated by the ethical norms that Muslims subscribe to. Nobody should, therefore, be apologetic about the type of questions raised in the rest of this book, e.g. what is the Islamic system of ethical values, and how do those values get translated into distinctive propositions regarding economic behaviour? To ignore such questions would be an ostrich-like posture that social scientists can ill-afford to assume even in the interest of their own intellectual health!

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CHAPTER 2

The Islamic Ethical System

The task of this chapter is to construct an axiom system that faithfully reflects the Islamic view of ethics. This is an essential first step in determining the rules of economic behaviour in an Islamic society. The Islamic view of life processes is unique not only for its predominant emphasis on ethical norms, but also because of its being "complete". Also, since this view is internally consistent, it can form the basis of scientific generalizations about an Islamic economy. However, to turn it into an operational tool of scientific analysis, an ethical philosophy must be reduced to a set of axioms, which can then serve as a point of departure for making logical deductions with respect to Islamically valid rules of social and economic behaviour. The four axioms identified in this chapter — Unity, Equilibrium, Free Will and Responsibility — together form such a logical system. Before we use this system for deriving the fundamentals of Islamic views on fruitful and legitimate economic behaviour, a brief explanation of each of its elements should highlight the distinctive character of Islam's ethical philosophy.

Islam's Ethical Philosophy

According to the Islamic ethical system, man occupies the central place in the Universe. He is not just one element in the vast expanse of God's creation but provides the *raison d'être* for all that exists: "See ye not how Allah hath made serviceable unto you whatsoever is in the skies and whatsoever is in the earth . . ." (31:20). He is a theomorphic being, with something God-like in him. The Qur'an testifies to man's exalted station in the Universe: "So, when I have made him and have breathed into him of My spirit . . ." (15:29). Hence it is his primary *duty* to realize in this world his theomorphic potentialities, and he will be held accountable if he does not: "Thinketh man that he is to be left aimless?" (75:36). To enable him

to perform this Divine mission, Islam looks at man as a "free" agent, invested with the responsibility that normally goes with freedom. The concept of human freedom and responsibility that Islam presented to the world at the beginning of the seventh century A.D. relates primarily to man in his individual capacity: "Your creation and your raising (from the dead) are only as (the creation and the raising of) a single soul" (31:28). By virtue of his freedom, man has the potentiality of becoming God's vicegerent on earth, of walking where angels fear to tread, and of ultimately getting crystallized into immortality.¹ By the same token, he can deny God. At any rate, he is fully responsible for whatever he does both in this world and on the Day of Judgement: "And every man's augury have We fastened to his own neck..." (17:13).

In addition to this concept of the "individual man", there is also in Islam a clearly recognizable "collective man". As a collectivity, man is related to his environment and should also be seen from that perspective. He must provide for the sustenance of the poor, and is required even to lay down his life for the survival of the *Ummah* (i.e. Muslim Community). Although, according to the Islamic teachings, the "individual man" comes before the "collective man", at least "historically", there is an essential reciprocity between these two aspects of man. In the all-comprehending vision of Islam, everything must be assigned a proper place.² Within the unitary Islamic philosophy, man's individual and collective actions are merely facets of an "integrated" theomorphic being, who is simultaneously an extrovert as well as an introvert. Within this "homogeneous" being, the esoteric and the exoteric aspects of his life are linked together in an indissoluble chain. As a result, man in Islam does not suffer the

¹ It would be useful to clarify a philosophical fine point at this stage. According to the Islamic perspective, man does not lose his finitude to gain immortality. As Iqbal has profoundly remarked, "Whatever may be the fate of the man, Islam does not contemplate complete liberation from finitude as the highest state of human bliss" [5, p. 117]. Even when in full view of the infinite, as the Prophet (Blessings of Allah and peace be upon him) was during his terrestrial journey, man's finitude remained *distinct*, though not *isolated* from the infinite: the Holy Qur'ān testifies: "The eye turned not aside nor yet was overbold" (53:17). *Thus immortality comes to man "on his own terms", not by the loss of his identity.* It comes when the soul is allowed to grow to the limit, so that he lives on even in death. It is for this reason that the Holy Qur'ān pointedly notes that man's life mission is to let his soul "grow": "He is indeed successful who causeth it (the soul) to grow, and he is indeed a failure who stunneth it" (9:9-10).

² For the distinction between man as such and the "Collective Man", see Frithjof Schuon [11, pp. 26-27], and Khurshid Ahmad [1, Ch. 1].

"alienation" of the Hegelian-Marxian man.³ According to the Islamic perspective, man becomes "alienated" only when he fails to realize his theomorphic potential by letting the inherent unity within himself fall apart.

Islam has also shown to man the best way to realize his theomorphic potential. His moral, spiritual and secular activities must be fully integrated and unified to reflect one another. The remarkable thing about the Islamic vision is that it combines the soaring idealism of man's spiritual ascent with a deep concern for his worldly attachment, which, within specified limits, has also been willed by God. In this scheme, man's life and his action must conform to the all-pervading quality of *al-'Adl* (i.e. Equilibrium), of which social justice is only one aspect. Islam aims not so much at creating a society of saints — although the virtues and rewards of saintliness have been greatly extolled in the Holy Qur'ān — as at bringing into being a social milieu which is composed of "balanced" human beings, who unify their multifarious activities within the ethical limits prescribed by God. Hence, while every effort must be made to cure man of his weakness, his natural propensity to self-indulgence must not be altogether ignored. Islamic ethics are based on the clear recognition that the basic traits of man's nature can at best be *neutralized* at a personal level; they can never be *abolished* altogether on the plane of social existence. Islam offers to mankind not a set of idealistic improvisations but a perspective of certainty. No ethical system which suspends natural laws for the sake of some kind of hypocritical idealism can find any place in a revealed message; for only God knows His creatures best: "We verily created man and We know what his soul whispereth to him, and We are nearer to him than his jugular vein" (50:16).

Fundamental Ethical Axioms

The integrated, balanced and realistic view of man's nature and his social role, exclusive to Islam, can be summarized exactly by four ethical axioms: Unity, Equilibrium, Free Will and Responsibility.

³ According to the Hegelian-Marxian sociological perspective, the "universal" or the "total" man becomes a stranger and suffers "alienation" in the capitalistic societies through the division of labour, getting gradually sucked into the whirlpool of giant collective organizations. According to this philosophy, economic alienation is the root cause of man's alienation from his environment.

Unity

Islam's ethical system, which encompasses man's life on Earth in its entirety, resides eternally prefigured in the concept of Unity, which, in an absolute sense, relates only to God. However, in so far as man is theomorphic, he also reflects this Divine quality.⁴ Mankind is nothing but the receptacle of the truth, and must reflect His glory in all worldly manifestations: "We shall show them Our portents on the horizons and within themselves until it will be manifest unto them that it is the Truth" (41:53). Unity is both an all-exclusive and an all-inclusive concept. At the level of the absolute, it differentiates the Creator from the created, requiring unconditional surrender by all to His will: "The decision rests with Allah only, Who hath commanded you that ye worship none save Him" (12:40). On the plane of human existence, this concept also provides a powerful integration principle, for all mankind is united in submission to Him: "Say: Lo! my worship and my sacrifice and my living and my dying are all for Allah, Lord of the Worlds" (6:163). In a deeper sense, the concept of Unity constitutes the vertical dimension of Islam. It integrates, along a vertical line, the political, economic, social, and religious aspects of man's life into a homogeneous whole, which is consistent from within as well as integrated with the vast Universe without. Within the compass of one immaculate, divinely revealed Vision, Unity shows the interrelatedness of all that exists. In the Islamic view, which is perfectly co-ordinated and necessary, the Universe, life on earth, and man all relate to an all-embracing Unity, wherein the perceptible and the imperceptible, material abilities and spiritual potentialities coalesce to highlight the theomorphic character of man. Through the *direct* knowledge of all the things created, which alone makes a *unified* view possible, the dream of a humanity marching in unison towards the ultimate truth can be realized on earth. The integrating force that Unity⁵ is operates not only within a

⁴ It should be noted that there is nothing *anthropomorphic* in this argument, since man is the receptacle of God's Will and must therefore reflect His essential qualities. To deny this would be to maintain, in the words of Frithjof Schuon, that "there is no resemblance between the moon and its reflection in water, because if there were a resemblance, the moon would have to be liquid like water" [9, p. 127].

⁵ The integrative role of the concept of Unity is clearly laid out in S.H. Nasr [6, pp. 29–32]. See also his other book, [7]. However the most complete discussion of this concept in relation to the Islamic social system is given in Syed Qutb [8]. See also Khurshid Ahmad [1].

particular society but among various societies as well, pointing to the universal character of the Islamic message: "O mankind! Lo! We have created you male and female, and have made you nations and tribes, that ye may know one another" (49:13). Thus mankind has been united not only in the knowledge of God, but also in men's knowledge of each other. Indeed, the two modes of knowledge are facets of the common pursuit of the ultimate truth.

Logically related to the integrative function of Unity is the fact that it provides mankind with a perspective of certainty, which derives from a deep sense of the Divine Equation between God and man. Man's search for the truth cannot fail to be fruitful if he is guided by the One, the only One, Who knows the entire truth; indeed, is truth Himself. "Allah leadeth to the truth. Is He Who leadeth to the truth more deserving that He should be followed, or he who findeth not the way unless he (himself) be guided" (10:36). Such a perspective is bound to dispel both hesitation and doubt because a wisdom that is prefigured in the Absolute cannot fail to guide man on the right path: "And he whom Allah guided, he is led aright" (17:97). Furthermore, certainty reinforces and cements the integrative force by informing it with a sense of the mission and with the assurance of its ultimate fulfilment.

Equilibrium

In addition to the vertical dimension, *al-'Adl*, which in a deeper sense denotes a balance of forces of Equilibrium, constitutes the horizontal dimension of Islam.⁶ At the absolute level, it is the supreme attribute of God; in fact, its denial constitutes a denial of God Himself. It follows that, at the relative level, the quality of Equilibrium must also characterize all His creation which must reflect His qualities. According to this precept, the Islamic view of life derives from a Divine perception of an all-pervading harmony in the Universe. "Thou (Muhammad) canst see no fault in the Beneficent One's creation; then look again: Canst thou see any

⁶ This dimensional characterization of Islam is briefly noted, but in a different context, by Frithjof Schuon [11]. See also another work by him [10]. In yet another work he notes: "It is the aim of Islam to combine the sense of the absolute with the quality of Equilibrium" [9, p. 23]. To avoid confusion, the reader should carefully note that the word Equilibrium has been used in this book in a very special sense denoted by *al-'Adl*. To the possible objection that *al-'Adl* means "Justice" and not Equilibrium, there is a simple answer: if justice is introduced everywhere, which is what Islam would insist upon, then a delicate balance – that is Equilibrium – will hold *throughout* such a society.

rifts? Then look again and yet again, thy sight will return unto thee weakened and made dim" (67:3-4). Indeed, Divine perfection, reflected in the quality of Equilibrium, exists in the very order of the Universe which hangs together in a delicate balance: "It is not for the sun to overtake the moon, nor doth the night outstrip the day. They float each in an orbit" (36:39).

Within the homogeneous whole that life is in the Islamic perspective, its various elements must be equilibrated to produce the best social order: "He hath created everything, and hath meted out for it a measure" (25:2); and "Lo! We have created every thing by measure" (54:49). Human existence itself carries all the basic life-giving qualities in an "undifferentiated equilibrium", so that any rupture of it is the negation of life itself, and therefore a positive evil.⁷ It follows that the property of Equilibrium not only obtains, but must be achieved through conscious purpose if it already does not exist: *it is not only a property but also a necessity*. Thus Equilibrium, or social harmony, is not so much a static property in the sense of a plea for the *status quo* as a dynamic quality releasing powerful forces against evil.⁸ Equilibrium must exist in our individual lives as well. The innermost of each individual, itself a living tabernacle of truth, is unified with it vertically as a homogeneous whole and is also equilibrated with respect to the elements within this whole. Within ourselves there is a world of errant desires and erupting ideas which must be contained and held together in correct proportions to produce a just human being. "O Ye who believe! Forbid not the good things which Allah hath made lawful for you, and transgress not. Lo! Allah loveth not transgressors" (5:87).

It may be noted here that the term Equilibrium, as used here, carries with it definite *normative* underpinnings. On the plane of

⁷ In fact, in an historical perspective, Islam itself represents a providential synthesis, equilibrating perfectly and finally the various aspects of the Divine Message. Frithjof Schuon has remarked: "The equilibrium between the two Divine aspects of Justice and Mercy constitutes the very essence of the Mohammedan Revolution, in which it rejoins the Abrahamic Revolution" [10, p. 96]. This also explains the logic of the Qur'anic injunction: "So follow the religion of Abraham, the upright" (3:95). For the religion of Abraham represented an equilibrium between the exoteric and the esoteric, between Mercy and Justice, a balance which Islam sought to re-establish.

⁸ In a deeper sense, this is what *Jihād* (Literally: Struggle) denotes. It includes waging war not only against the infidels, but also against the evil both within and without ourselves. Indeed, the Holy Prophet (Blessings of Allah and peace be upon him) declared the fight against evil within one's self to be a higher form of *Jihād*, which points to the dynamic quality of the Islamic message.

social existence, it denotes a binding moral commitment of the individuals in any society to uphold a delicate balance in all aspects of their lives. Hence, this concept must be distinguished from the one used in mechanics or economics where it has no normative or ethical significance. Islam not only emphasizes the fact of Equilibrium but also insists on the *quality* of Equilibrium.⁹ In a special sense, it represents a first-best conglomeration of natural and social forces to reproduce in human life that harmony which already exists in Nature: "We verily sent Our messengers with clear proofs, and revealed with them the Scripture and the Balance, that mankind may observe right measure . . ." (57:25). In the Islamic view of social dynamics, the rise and fall of civilizations can be seen in terms of their "distance" from the universal Equilibrium. It is easy to indulge in excesses; but to maintain a delicate equilibrium in human affairs stretches human ingenuity to the maximum, and brings out the best in man in terms of forbearance and self-control. Nations which cannot act judiciously are relegated to the backwaters of history. The eternal law of Equilibrium admits of no exceptions: "And We set a just balance for the Day of Resurrection so that no soul is wronged in aught. Though it be of the weight of a grain of mustard seed, We bring it" (21:47).

Free Will

One of the most original contributions of Islam to social philosophy is the concept of a "free" man. Only God is absolutely free, but, within the limits of His scheme of Creation, man is also relatively free.¹⁰ Contrary to what has been propagated in non-Muslim circles, man in the Islamic perspective is not chained to predestination in the literal sense. Having been given the faculty to choose, he has the freedom either to become God-like by realizing his theomorphic character, or, using his Free Will, to deny God. This freedom to accept or reject whatever is on Earth followed from man's acceptance, even before creation, of a burden which no-one else could

⁹ In economics, it is possible to obtain equilibrium solutions which are completely "trivial" from a normative point of view. However, in the Islamic perspective, such solutions are simply not admissible.

¹⁰ Being relative in no way diminishes the quality of human freedom. As Schuon has profoundly pointed out, "God alone has absolute freedom, but human freedom, despite its relativity — in the sense that it is relatively absolute — is nothing other than freedom any more than a feeble light is something other than light" [11, p. 14].

endure: "Lo! We offered the trust unto the heavens and the earth and the hills, but they shrank from bearing it and were afraid of it. And man assumed it" (33:72). True, God's omniscience encompasses all man's actions throughout his sojourn on Earth, but man's freedom is also God-given.

By accepting to act as the receptacle of God's power of discretion, man has been assigned to the most distinguished niche in the Universe.¹¹ *His theomorphic character, combined with Free Will, sanctifies in the clearest possible terms the principle of human freedom, which is innate in human nature.* The God-given freedom of man not only cannot be taken away from him, but must also be safeguarded through the creation of institutional safeguards that prevent its desecration by unnatural authoritarianism. Thus no Magna Charta is required to confer on man his God-given freedom. By the same token, any such attempt to relieve man of the burdens of slavery becomes ennobled in the eyes of God, simply because it constitutes a fulfilment of the Divine purpose. It also follows that to deprive man of his natural freedom is to degrade him below his God-given stature, producing disequilibrium in society. Any such act is, therefore, a cardinal sin. It should be emphasized that human freedom applies both to the "individual man" and to the "collective man", emphasizing a correct balance between the two. In this respect, the Islamic concept of freedom differs from that propounded by such Western social philosophers as Adam Smith, John Stuart Mill and Quesnay. According to them, the individual's (almost unlimited) right to private property provides a set of institutions which can make the maximum contribution to social good. However, Islam does not accord unqualified sanction to an individual's right to private property, because all property belongs to

¹¹ The emphasis on the central importance of the individual, not only in the society but in the Universe, is one of the hall-marks of the teachings of Islam, which makes it the most progressive religion of the world. Iqbal has very lucidly brought out this aspect of Islam. His deductions are based on three Qur'anic propositions about the place of the individual in the Universe: (i) "that man is the chosen of God", (ii) "that man, with all his faults, is meant to be the representative of God on earth", and (iii) "that man is the trustee of a free personality which he accepted at his peril" [5, p. 95]. Ameer Ali also emphasized this aspect of man: "Arabian philosophy, nurtured afterwards in other cradles, drew its first breath in the school of Medina. The freedom of human will, based on the doctrine that man would be judged by the use he had made of his reason, was inculcated in the teachings of the Master, along with an earnest belief in a supreme power ruling the universe" [2]. See for a similar view Schuon [11] and S.H. Nasr [6].

God and man is only His trustee on earth. Hence, an individual does not have an exclusive "natural" right to what he earns, and has even less to what he can inherit.* Furthermore, the roots of human freedom, according to Islam, cannot be traced to an uncertainty about who knows best, but flows naturally and serenely from a perspective of certainty: "Allah knoweth, ye know not" (2:216). According to Western social philosophy, individuals should be allowed the freedom to choose because no one individual has the exclusive right to reason, and hence what is best can be discovered only by a process of trial and error.¹² In the classical economic model, this works out through atomistic market behaviour of the individual, each insignificant, coupled with the institution of private property. The inadequacy of this argument can be shown by pointing out that what the system of free markets can at best achieve is to lead the competing individuals on to the "efficiency locus" – i.e. a configuration of a whole set of points which are consistent with the utility-maximizing behaviour of the freely acting individuals. However, not every point on this locus coincides with the best social welfare. To discover the "bliss" point, a social welfare function must be found, representing the preferences of "who knows best".¹³

In the Islamic framework, valid deductions based on the Qur'an and the *Sunnah* condition the preferences of those who know best. Thus inevitably, by the sheer logic of Islamic reasoning, ethical constraints delimit the area of choice both for the "individual man" and for the "collective man". This perspective is basically much more unified, and productive of better social results by comparison with the one which effects the marriage of unconstrained selfish interests of the atomistic market agents with those of "who know best". It is for this reason that there is no warrant in the Islamic system for De Tocqueville's fears that conscious attempts to make people equal may lead to "a new form of servitude". For if human freedom is God-given and individuals act in accordance with the ethics of this freedom, the element of coercion involved in reconciling private and social interests must be minimal. By the same token, it follows that if such a conflict between private and social interests does exist then it must be removed to satisfy the *preconditions* of an Islamic society.

*These matters are discussed in chapter 6.

¹² For an eloquent exposition of this point of view, see F.A. Hayek [4, esp. Chapter 1].

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Responsibility

Logically related to Free Will is the axiom of Responsibility.¹⁴ It sets limits to what man is free to do by making him responsible for all that he does: "Whoso interveneth in a good cause will have the reward thereof, and whoso interveneth in an evil cause will bear the consequences thereof" (4:85). It follows that the cult of unethical, unbridled individualism is also not allowed in Islam. Even pure logic should convince us that unlimited freedom is an absurdity: unlimited freedom implies unlimited responsibility. This is a contradiction because both these statements cannot be true at the same time. Freedom must be counter-balanced by responsibility if only to satisfy the dictates of Nature's Equilibrium. Man, having opted for the power to choose between good and evil, must endure its logical consequences: "Every soul is a pledge for its own deeds" (74:38). Once God has shown the way, the responsibility for going astray is wholly man's and he will have to suffer for his wayward behaviour: "Say: O mankind! Now hath the truth from your Lord come unto you. So whosoever is guided is guided only for (the good of) his soul, and whosoever erreth erreth only against it. And, I am not a warder over you" (10:109). Because of the universal quality of *al-'Adl*, every individual must be held responsible for his actions. No-one can escape the consequences of his misdeeds just by pointing to a convenient scapegoat: "Each soul earneth only on its own account, nor doth any laden bear another's load" (6:165).

Not only that. Man has also been held responsible for the evil that goes on around him. Accordingly, man has been forewarned: "And guard yourselves against a chastisement which cannot fall exclusively on those of you who are wrongdoers..." (8:25). Except for the sick, the children and women, the rest cannot escape Allah's retribution on the excuse that they were too weak to stop evil in the society. If one can't do anything about what goes wrong in a particular society, then he is commanded to migrate from that society or he, too, will be taken in: "Lo! as for those whom the angels take (in death) while they wrong themselves, (the angels) will ask: In what

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The Doctrine of Responsibility in fact constitutes a dynamic principle in relation to human behaviour.¹⁵ Man must evolve to reach perfection; but evolution is a negation of the *status quo*, and requires that no-one should be chained to his past or contained within the confines of his present. Islam rejects all appeals to traditional mores as a justification for man's deviation from the right path. Blind imitation of the ways of one's forefathers has been condemned in the Holy Qur'an in no uncertain terms. An inglorious past cannot be invoked to justify the evils of the present: "And if it be said unto them: Follow that which Allah hath revealed, they say: Nay but we follow that wherein we found our fathers. What! Even though the devil were inviting them unto the doom of flame?" (31:21). At the same time, once again reflecting Islam's commitment to social justice, man "today" has been completely absolved of the responsibility of what happened "yesterday": "Those are a people who have passed away. Theirs is that which they earned, and yours is that which ye earn. And ye will not be asked of what they used to do" (2:134). Man should be forward-looking rather than backward-looking, because it is God's Will "That ye shall journey on from plane to plane" (84:19). Going a step further, the entire responsibility for not ushering in a better future rests entirely on man's shoulders: "Lo! Allah changeth not the condition of a folk until they (first) change that which is in their hearts..." (13:11). It should, therefore, be clear that fatalism, implied in predestination, is no part of the Islamic message. Instead, Islam replaces a static outlook with a healthy dynamism.¹⁶ A free individual is not one who is insensitive

¹⁵ It is interesting to note at this point the difference between our point of view regarding the dynamic nature of an Islamic society and that held by other Muslim authors. For instance, Iqbal singles out *Ijtihad* to be the primary dynamic force – or "the principle of movement", as he calls it – in the Islamic system [5, Ch. 6]. However, this is only a partial view. The dynamic force instead is the *responsibility* of the individual to maintain the quality of *equilibrium* in an Islamic society. *Ijtihad* is only one of the means to restore equilibrium, *at the intellectual plane*; the other is *Jihad*, which does this at the *social plane*, the latter being the more basic of the two.

¹⁶ Verses in the Holy Qur'an such as: "Thou exaltest whom Thou wilt and Thou abasest whom Thou wilt. In Thy hand is the good. Lo! Thou art Able to do all things" (3:26), do not absolve mankind of what they do. This verse is instead a statement of complete freedom of the Absolute; but Divine freedom cannot be confused with arbitrariness. Divine Will does

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Summary

The distinctive character of Islamic ethics rests largely on its conception of man in relation to God, his own self, the Universe and the society. Through the essential multidimensionality of an integrated personality, Islam points to a responsible man who is free to realize his theomorphic character. He must be guided by a conscious purpose, exercising to the full his powers of discretion in a balanced way. In this perspective, human behaviour takes on a new character in that it has been providentially freed from any sense of "guilt". By virtue of his distinctive qualities man has been "aligned" with his environment, indeed with the Universe at large. As a consequence, within the panoramic Islamic vision, man can neither go adrift by aimlessness nor be "alienated" from his surroundings. At the same time, his unaltruistic behaviour is tempered because Islam requires man to be sensitive to his environment, for the betterment of which he bears full responsibility. Furthermore, he is not allowed to be tradition-bound: he has no responsibility for the past in which he had

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Fundamental Considerations

PART II

ISLAMIC ECONOMIC SYSTEM

"Unto Allah belongeth whatsoever is in the heavens and whatsoever is in the earth"

The Holy Qur'an (3:129).

CHAPTER 3

Fundamental Considerations

The approach adopted in this book for determining Islam's view on economics is one of scientific objectivism. In the previous chapter, we sought to identify a set of axioms which adequately summarize Islam's ethical stance on life processes in general. In this and the subsequent chapters, this axiom system will be used to derive, through the process of logical deduction, the essentials of Islamic economics. Through a consistent application of this analytical technique can also be established the Islamic or un-Islamic nature of the existing economic systems and doctrines.

The axiomatic method used in this book acts both as an effective integration principle and a "rejection" mechanism. While, according to it, incompatible elements must be cast out from the realm of ideas, the best of human knowledge has to be assimilated into the corpus of Islamic doctrines, since it is the common heritage of all mankind. The Islamic approach to life is not at all Spenglerian, according to which different cultures grow up in veritable water-tight compartments, with no interaction among them. In sharp contrast to this unnatural isolationism, the Islamic view is evolutionary with respect to the acquisition of knowledge. Islam makes it obligatory on Muslims to look around and cull the best from what life has to offer. Indeed, this was the attitude of the Muslim philosophers in the Middle Ages who learned all there was to learn from the then existing scientific knowledge and transmuted it into the Islamic frame of thought.¹ The modern Muslim social scientist, in his efforts to evolve a school of Islamic thought, will also have to be eclectic as well as particularistic. Any distinctive body of doctrines is known not only by what it includes, but also through that which is excluded from it.

¹ See Iqbal [3] for the essential *empirical* character of the Muslim contribution to knowledge in the Middle Ages.

The Islamic economic system rests firmly on four basic hypotheses:²

- (i) economic activity is indissolubly linked, through Unity, with man's ethical environment;
- (ii) by virtue of the basic quality of Equilibrium, in the sense explained above, there must obtain a "just" balance among the basic production, consumption and distribution relations;
- (iii) Free Will, translated onto the economic space, requires that individual economic freedom and state control be suitably combined to reflect the distinctive Islamic concept of human freedom; and
- (iv) the axiom of Responsibility dictates a conscious policy of redistribution and resource transfers among various classes and groups of the society. It also implies a financial relationship between the lender and the borrower which takes explicit cognizance of the essentially risky nature of economic actions.

This chapter spells out these hypotheses and their logical consequences for the distinctive type of economic behaviour required of the "economic agents" in an Islamic economy.

Economic Activity and the Unity Axiom

An important aspect of economic theorizing has been the exclusion from consideration of the effect of "exogenous forces", ethical factors in particular, on the process of economic change.³ Even when these factors are allowed to vary, within the framework of antiseptically constructed models, they produce very weak reverberations on the equilibrium values of economic variables. In the unitary Islamic perspective, such a procedure is not acceptable. Islam sets out to heal, through a conscious unifying process, the current schism between ethics and economics. Such a synthesis will have far-reaching consequences for economic behaviour in an Islamic society. Firstly, the character of the "Economic Man", as the term is used in economics, will be completely transformed.⁴ His

² As a technical note: to draw valid deductions, a few "hypotheses" are normally added, as done in the text, to explain more fully an axiom system. This procedure is strictly scientific in so far as the fulfilment of these hypotheses causes such conclusions to be true as do not directly follow from the axioms. For an excellent discussion of these matters, see M.C. Gemignani [1].

³ See Hirschman [2, esp. Introduction].

⁴ It should be noted that this concept, as used in economics, by no means implies that such a "man" does in fact exist. The term is used as a logical abstraction to highlight a simulated model of economic activity, in which man is the principal actor.

utility-maximizing behaviour will be subjected to two distinct constraints: (i) the usual feasibility constraint, i.e. whether the commodity bundle is producible; and (ii) the *allowability constraint*, exclusive to Islamic economics, which classifies as "bads" commodities the consumption of which has been ordained to be zero in an Islamic economy. This also implies, in terms of neo-classical microeconomics, that in such cases the "free-disposal" assumption can't hold. As a result, the commodity space will be "defined" differently in an Islamic economic system than in other economic systems, with a definite ethical cost assigned to the production of such bads.

Secondly, even within this "contracted" commodity sub-space, the desire of an individual to consume commodities may not be – or, more accurately, will not be – totally "insatiable" with respect to every commodity by virtue of the Qur'ānic commandment, "... eat and drink, but be not prodigal" (7:31). It follows that, when the neo-classical insatiability assumption is suitably modified, the utility-maximizing consumption basket will be different in an Islamic economic system than in any other economic system.⁵ Not only that. The profit-maximizing behaviour of the Economic Man will also have to be constrained to produce just such a consumption basket.

Thirdly, as is well-known, a "competitive economy" has two characteristics: (i) prices are parametrically given; and (ii) specific assumptions are made regarding the ownership of resources and the manner in which production is organized.⁶ It should be obvious that once the Islamic ethical biases regarding resource ownership are fully integrated with economics it must profoundly influence the "character" of competitive equilibrium (see the discussion under the next heading below). The "contents" of the efficiency locus will also be different since the commodity mix, coming out of the interaction of consumers and producers, is bound to be different in an Islamic economy, by comparison with that obtaining under non-Islamic economies. Furthermore, the social welfare function in an Islamic society, reflecting a specific *kind* of social choice in an Islamic

⁵ See Anas Zarqa [9] for a detailed discussion of the characteristics of what he calls the "Homo Islamicus" as opposed to the "Homo Economicus". The main difference between these two prototypes, according to Zarqa, is that the consumption behaviour of the former is deeply influenced by a consideration of the penalty or reward in the life after death.

⁶ See J. Quirk and R. Saposnik [8, Chapter 3].

economy, will pick out a point on this efficiency locus consistent with its ethical norms.

Fourthly, thanks to the integration of economics with ethics, the Economic Man will also have to take into account the consumption and production behaviours of others in the society. Thus, contrary to one of the basic assumptions of the neo-classical utility analysis, he can no longer remain incurably "selfish" in his consumption behaviour; nor can he produce independently of what others are producing: *the interdependence of utility functions and production functions must be explicitly taken into account*. For, in the Islamic perspective, the Economic Man must simultaneously be an individual as well as a collective entity. The Islamic ethical principles not only determine individual choice and collective choice, but also provide a principle of integrating the two.

Economic Structure and the Equilibrium Axiom

The absolute requirement that the quality of Equilibrium holds in all aspects of man's activity will be one of the most important determinants of economic behaviour in an Islamic economy.⁷ Firstly, the basic consumption, production and distribution relationships will stand in a certain balance in order to avoid the concentration of economic power in a few hands. It follows that exploitative monopolies, on both sides of the market, should find no place in an Islamic economy. An obvious exception to this rule will be public utilities where the existence of sizeable "external" economies tends to determine the plant size. Hence, state enterprises may become economically essential from both the efficiency and the welfare points of view. However, in so far as atomistic behaviour is economically and socially desirable, neither the producers nor the consumers can lower social welfare by dictating price and output

⁷ Social equilibrium must be maintained not only in material terms (e.g. an equitable distribution of wealth), but also in terms of an equitable distribution of self-respect between the haves and the have-nots. The rich are not allowed to exchange their money for the self-respect of the poor: "O ye who believe! Render not vain your almsgiving by reproach or injury, like him who spendeth his wealth only to be seen of men and believeth not in Allah and the Last Day. His likeness is as the likeness of a rock whereon is dust of earth; a rain-storm smiteth it, leaving it smooth and bare" (2:264). This Qur'anic verse once again testifies to Islam's insistence on the *quality* of equilibrium for achieving a viable socio-economic framework, which combines economic progress with social and spiritual happiness.

configurations and by keeping production level below the socially optimal level.

Secondly "states" of the economy not consistent with the Islamically first-best distribution of income *and* wealth will be ruled out. Islam unequivocally rejects the closed circle of income and wealth getting narrower at each turn: "[Let] it (i.e. wealth) become not a commodity between the rich among you" (59:7).⁸ In technical parlance, an Islamic system would insist, at a given point in time, on maximizing "total" welfare, and not just (pareto-optimal) marginal welfare, stipulating that income distribution must also be the first-best. (In a dynamic context, this restriction would require that the "initial" conditions should satisfy this requirement.) The *ideal* Islamic position in this respect follows directly from the fact that, by virtue of man's theomorphic character and to satisfy the dictates of Equilibrium, the marginal social significance of every individual in an Islamic society must be the same. Hence every individual's happiness should have the same value from a social point of view. Assuming that the law of diminishing returns applies to all "goods", the marginal value of extra income must be more for the poor than for the rich. Hence, to maximize total satisfaction in the society, it is essential that income equality holds in an absolute sense. By the same token, a rise in the degree of income inequality will tend to diminish overall happiness and satisfaction. In other words, from the Islamic point of view, a society with an equal income distribution is superior to a society with an unequal distribution of income, even though the average income levels are the same in the two societies.⁹ It follows that gross inequalities of income and wealth are contrary to the Islamic ideal. To attain this ideal, Islam prohibits the hoarding of wealth: "Who hoard their wealth and enjoin avarice on others, and hide that which Allah hath bestowed upon them of His bounty. For disbelievers We prepare a shameful doom" (4:37). At the same time, Islam condemns ostentatious consumption, and extols the virtues of giving: "Spend your wealth for the cause of Allah, and be not cast by your own hands to ruin; and do good. Lo! Allah loveth

⁸ Although this verse originally referred to the distribution of spoils of war among the faithful, there is a consensus among Muslim jurists that the formula prescribed here equally refers to distribution of *all* types of wealth among the Muslims.

⁹ For a general discussion of such reasoning, see Oscar Lange [5]. This point of view is in perfect accord with the views of pious Muslims like Abu Dharr, a close companion of the Holy Prophet (Blessings of Allah and peace be upon him), who believed in an absolute equality of income.

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the beneficent" (2:195). By effecting a proper balance between saving, spending and voluntary giving, Islam seeks to push the society towards the ideal state – that is, *what Islam considers to be the ideal state*.

Thirdly, a direct corollary of this heavy egalitarian bias is that the individual's unlimited right to property has no warrant in an Islamic economic system – all the more so because no economic programme, aiming at social justice, can succeed without substantially pruning the private property system. Not only this. All institutions that promote gross inequalities of income and wealth – e.g. the institution of interest, which feeds on private property and strengthens it in turn – will have to be eliminated, albeit gradually, in a fully-fledged Islamic economy. The basic rationale for this point of view is that, in the Islamic perspective, all property belongs to Allah: "Unto Allah belongeth whatsoever is in the heavens and whatsoever is in the earth" (3:129). Hence, man, being God's vicegerent, holds in trust whatever is on earth.

Institutional Framework and the Free Will Axiom

The Free Will axiom implies that appropriate institutional arrangements should be made to guarantee economic freedom to individuals, within the specified ethical constraints. Does it then follow that atomistic competition, i.e. *laissez faire*, approximates the Islamic Ideal? This is a complicated question because the legitimacy of specific market structures in different societal contexts can only be established by actual observation and empirical verification. *A priori* reasoning can help to provide only broad guidance. However, following from the "first principles", there are a few points that indicate a negative answer to this question. Firstly, as pointed out in Chapter 2, the Islamic concept of human freedom is consistent with a substantial role of the State in an Islamic economy. However, this fact runs counter to the basic philosophy of pure and perfect competition, which is based on the dominance and the moral superiority of the "Invisible Hand".¹⁰

¹⁰ It is interesting to note that much of the mystery surrounding Montesquieu's Invisible Hand – an invisible force reconciling effortlessly the pursuit of selfish interest with social welfare, which is maximized under competitive equilibrium – largely disappears in an Islamic economy. This is because the unitary Islamic philosophy "conditions" individual preferences in such a way that they no longer conflict with public welfare. This conditioning comes about not unknowingly or accidentally, but as a result of a *conscious* regulation of man's economic activities, specifying not only the needs but also the means for achieving them.

Secondly, an explicit recognition of externalities in consumption as well as production will get sharper in an ethically-oriented society like Islam's than in those societies which claim to be ethically neutral. For instance, the resistance will be greater in such a society to the unethical behaviour of producers in setting up industries which cause serious damage to public health. As a result, the frequency and the magnitude of government intervention in an Islamic system will be greater, though much less coercive, than in a capitalistic system.¹¹ It follows from these considerations that, *even at a theoretical level*, the models of competitive equilibrium may not be of much use in "simulating" market behaviour in an Islamic economy.

Economic Behaviour and the Responsibility Axiom

The axiom of Responsibility gets translated into a distinctive behaviour pattern of the economic agents in an Islamic society. Since man has been assigned a clear responsibility to improve the quality of his socio-economic environment, an individual's consumption behaviour will not be exclusively a function of his own income; it must show an awareness of the income and consumption levels of other members of the society as well. Not only this. The consumption levels of different members of the society must also stand in a certain relationship which is *not* necessarily proportional to the level of an individual's earnings (see Chapter 5). Once again, state intervention becomes warranted, this time to effect a transfer of resources which should be sufficient to bring individual consumption behaviour in line with what is considered socially desirable in an Islamic society.

The Responsibility axiom alters in a fundamental way an individual's economic calculus by reference to what is "just". Firstly, in calculating the profit margins, wage costs must be such as correspond to that deemed to be a socially acceptable minimum in an Islamic society. The upper bounds of the profit margins are thus

¹¹ Atomistic competition fails to maximize social welfare when substantial external economies are present. State intervention is called for in such cases because a systematic application of the marginal pricing rule by the private producer will lead to an underexpansion of social output. Furthermore, as pointed out in Chapter 9, free competition will indeed exacerbate social injustice when the society suffers from sharp differentials in income and wealth.

specified, particularly because *wages must be fixed in advance*.¹² Secondly, the economic return to the lenders of capital must be calculated on the explicit understanding that its magnitude cannot be predicted with a zero probability of error and *cannot*, therefore, be fixed in advance. In such cases the economic landscape in an Islamic society will be one wherein one-to-one correspondence between economic actions and their outcomes may not necessarily obtain. This implies that an explicit rule of economic behaviour should be laid down to regulate the magnitude and frequency of uncertainty in an Islamic economy.¹³ Thirdly, Islam prohibits all aleatory deals – called *gharar* in Islamic literature – in which the buyer is not always in a position to predict the full financial consequences of a transaction. A classic example is the advance sale of the expected fruits of a tree which has not yet borne fruit. In this case, the buyer cannot be made to suffer if the fruits don't grow or are destroyed by a natural calamity. Such economic transactions can easily be extended to cover most speculative deals.

Summary

It should be quite clear that the fundamental ethical axioms – Unity, Equilibrium, Free Will and Responsibility – yield an individual and a social outlook on economic life which, to say the least, are highly distinctive in character. On the theoretical plane as well as at the operational level, the “Economic Man” is differently defined in an Islamic economy with respect to what is considered rational action. Also, “his” freedom of manoeuvre is suitably curtailed to reflect the allowability constraint as well as the social requirement to produce the right kind of commodity mix. This has consequences both for the commodity “sub-space” in which the Economic Man can legitimately (from an ethical point of view) operate and for his utility-maximizing and profit-maximizing behaviours. The quality of Equilibrium will dominate the economic landscape in an Islamic economy, ruling out both exploitative market structures and the “selfish” atomistic behaviour of the

¹² Hiring a person for an undefined and indeterminate wage is not allowed in Islam.

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economic agents. While all steps will be taken to preserve God-given freedom, legitimate constraints, reflecting the Responsibility axiom, will have to be introduced to ensure freedom for all. For man is not allowed in an Islamic society to remain blissfully ignorant of, or even indifferent to, whatever happens in the environment of which he is a part and to which he has a definite obligation. Islands of prosperity rising from a sea of poverty should not be an acceptable spectacle in an Islamic economy. It follows that explicit state control of individual economic behaviour for bringing consumption levels and production patterns in line with what is socially just should be a normal “fact of life” in such a society.

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CHAPTER 4

A Comparative Perspective

To bring into sharp focus the main features of the Islamic economic system it may be useful to compare it with the existing economic systems, viz. capitalism, socialism and the welfare state. Such a comparative analysis is all the more essential because the Islamic system has been variously identified with capitalism, socialism, and even with a welfare state. Such attempts are not very helpful because the resulting intellectual ambivalence obscures the vision of a new Islamic economic order. Mistaken as they are, these superficial impressions cannot be dispelled just by focusing on isolated dissimilarities between economic systems; for such an argument can be quickly demolished by citing even more persuasive inter-system similarities. As pointed out above, economic systems may have some, though not all, common components without losing their title to originality, which can be established only by reference to the "first principles". Within the framework of the axiomatic approach, it should be possible to establish analytically, not by mere rhetoric assertions, the distinctive character of the Islamic economic system, steering clear of its misplaced and confusing associations with other economic systems.

Socialism

Is the Islamic framework socialistic? The temptation is great to give at least a partially affirmative answer. Not only in theory but also in practice, socialism has effectively come to grips with the problem of ensuring an equitable distribution of income and wealth among various classes of society, inducing social equilibrium. It has abolished the institution of private property, and, with it, the parasitic class of feudal lords has been effectively routed. The equalization of the opportunities of education, medical care, etc. has been carried the farthest in socialistic countries. Socialistic societies

also induce a sense of discipline and social purpose, which *appears* to be in conformity with the Islamic emphasis on collective responsibility. Furthermore, consistent with the Islamic ideal for the rulers, there is an air of austere simplicity about the ruling class in socialistic societies.

However, despite these and some other apparent similarities in certain details, socialism, as a self-contained system, is *not* Islamic. The arguments against the system – indeed, against all the non-Islamic systems – are mostly ethical, which, in the Islamic perspective, are decisive. Firstly, socialism, by making man's material pursuits the basis of social structures, negates the Islamic concept of Unity. This is not to say that ethics have no place in the socialistic philosophy; only they have been made subservient to economics. This is exactly the reverse of what Islam maintains. It follows that the societal configurations emerging under the two systems must differ fundamentally from each other. Secondly, the socialistic historical vision diverges sharply from Islam's. The rhythm of social progress, under the socialistic scheme, is supplied by cataclysmic dialectics – the gyrating triad of thesis, antithesis and synthesis, running through time and space with an unrelenting force, fed by mutual hatred and class war.

In sharp contrast, human societies, in the Islamic perspective, progress along the "straight path" of social harmony, which even the differences of sex, colour, and nationalities tend to solidify: "O mankind! Lo! We have created you male and female, and have made you nations and tribes that ye may know one another" (49:13). At the same time, Islam recognizes that if and when the universal law of Equilibrium is obstructed, strife and struggle would take place pitting the oppressed against the oppressors. Whenever that happens, the Islamic bias will invariably be on the side of the poor, the weak, and the oppressed: "And We desired to show favour unto those who were oppressed in the earth, and to make them examples and to make them the inheritors; And to establish them in the earth" (28:5–6). Not only that. The Holy Qur'ān has issued a stern warning to those on the side of justice that they must discharge their compulsory duty to help the poor against the oppressors: "How should ye not fight for the cause of Allah and of the feeble among men and of the women and the children who are crying: Our Lord! Bring us forth from out this town of which the people are oppressors! Oh, give us from Thy presence some protecting friend! Oh, give us from Thy

presence some defender!" (4:75).¹

However, an ideal state, according to Islam, is that of social harmony; and from that point of view, class struggle is the exception rather than the rule.² It follows that, in terms of its character, the Islamic approach to Equilibrium is qualitatively and conceptually different from the Marxian vision of the inevitable dialectic synthesis, precisely because of the wide gulf between the ethical perceptions of the two systems.³ Furthermore, the *quality* of Equilibrium is different under the two systems: while socialism ensures a fair distribution of income and wealth, it concentrates real economic and political power in the hands of the State.⁴ Thus the overall impact of socialistic reform on Equilibrium is indeterminate: the concentration of all power in the hands of the ruling élite destroys social equilibrium that socialism seeks to promote through an equitable distribution of income and wealth. Islam, on the other hand, insists on an equitable division of economic and political powers among different sections (*not classes*) of the society.

Thirdly, the Islamic concept of a free man, based on the axioms of Free Will and Responsibility, does not survive under the heat of

¹ While doing so, no-one is allowed to exceed limits in the name of vengeance. Once the truth has been driven home, forgiveness is better than vengeance; "If ye punish, then punish with the like of that wherewith ye were afflicted. But if ye endure patiently, verily it is better for the patient" (16:126). The essential thing is to re-establish the universal law once it is disturbed by the wrongdoers. No more is required.

² Compare Chapra who points out that "The fundamental thing is the co-operation, mutual understanding, acquaintance and harmony on the lines set by the Divine Law, and whoever deviates from this principle must be brought back to it" [3, p. 122]. However, he attributes this Law to the Divine Will, while throughout this book it is shown to rest on *al-'Adl* (Equilibrium), a quality which is innate in the Divine Nature.

³ Since man is free, he can ensure Equilibrium as well as violate it. When the latter happens, class war ensues. Islam does not construe this latter possibility as a universal Law, but as a deviation from it. However, Islam and the Marxian philosophy are at one in focusing on the cause of the downtrodden, the poor and the weak.

⁴ Lindbolm notes that, unlike economic equality, communist countries "never aspired to political equality and have in fact disclaimed it in order to justify concentrating political authority in a ruling élite" [5, p. 266]. However, in all fairness it should be pointed out that, as expounded in the Communist Manifesto, the Marxian vision was not of a monolithic State. In fact, Marx predicted that the proletarian revolution will lead to a classless society, bringing to an end its antagonistic character. He predicted the "withering away of the state" in the long run – a move towards social equilibrium. However, the latter-day theorizing of Lenin and Stalin, together with the reality, has rejected effectively the Marxian perception. See Raymond Aron [1]. In sharp contrast, the State *never* withers away in the Islamic vision but remains very much there to bridge the gap between freedom and responsibility and to help the centripetal forces of equilibrium.

collectivization carried to unnatural extremes in socialistic societies. Several traits of the socialistic philosophy have contributed to the "death" of the free man. At a philosophical level, historical determinism, an integral part of socialistic thought, puts the individual way down its value scale. Man is merely a cog in the historical machine, which moves on relentlessly and independently of what he may do about it. According to Marxian philosophy, human relations are independent of man's will.⁵ On the economic plane, this philosophy carries over into a complete socialization of *all* the means of production, in which individual initiative plays little or no part.⁶ Even the mobilization of manpower, a great achievement of the socialistic countries, is brought about through draconian measures like concentration camps. On moral grounds, man is seen in the socialistic perspective as committed to bearing an excessive collective responsibility to the point of destroying human freedom. On the other hand, the Islamic emphasis on Free Will liberates man from the clutches of historical determinism. *In the Islamic perspective, historical determinism is not independent of human will, which, through its irresistible force, can change the course of history.*⁷ Thus ideas of men, who realize their theomorphic character, become a determining force in social dynamics.

Islam balances Free Will and Responsibility, and puts them within an overall perspective which accepts man as having been born free. As such, it rejects unnatural harshness in work; "Allah would not place a burden on you, but He would purify you and would perfect His grace upon you, that ye may give thanks" (5:6). Man needs leisure as much as work to keep a proper balance between his material and spiritual pursuits: "And behold, with every hardship comes ease; verily with every hardship comes ease; Hence, when thou art relieved (from distress), remain steadfast, and unto thy

⁵ Marx clearly pointed to the subservience of human will to the conditions of human existence, which are in turn determined by production relations in the given society: "It is not the consciousness of men that determines their existence, but, on the contrary, their social existence determines their consciousness" [6, Preface].

⁶ As Bertrand Russell [7] has pointed out, "there can be no adequate individual freedom where the state is all-powerful, even if the state be a socialist one".

⁷ It is no doubt true that, as Iqbal has noted [4], under the influence of the Umayyads, a kind "of morally degrading fatalism" was in fact promoted to support their vested interests. However, such a vicious doctrine had nothing to do with Islam, which accepts nothing that is unjust, even if it is an accomplished fact. See Chapter 2, *supra*.

Sustainer turn with love (94:5-8).^{*} Here is also a warning against indolence, irresponsibility and sloth; for when the chips are down, "...man hath only that for which he maketh effort" (53:39).

Capitalism

Is capitalism, then, any nearer to the Islamic Ideal? At the conceptual level, one can easily be trapped into the fallacious argument that as both capitalism and Islam reject socialism, capitalism may be nearer to Islam. One may then go on to point out formal similarities by noting that, like Islam, capitalism is also founded on a respect for individual freedom. Indeed, its political counterpart, democracy, seeks to provide an institutional framework which safeguards freedom of the individual while reminding him of his social responsibility.

And yet this reasoning is false because Islam rejects both socialism and capitalism, since it has a distinctive system of its own. Indeed, it can easily be shown that *if the Islamic ideology had prevailed in the 18th century, capitalism could never have come into existence.* According to Max Weber, the Protestant "ascetic ethics" not only condoned but glorified a kind of callousness towards society in the name of unlimited accumulation. Thus ethics, among other reprehensible traits, justified exploitative wages to secure high productivity and stressed obedient and diligent service to their cruel masters as the labourers' path to salvation.⁸ In sharp contrast, the Islamic ethical values would not have permitted the exploitation of the poor by the rich; nor would it have condoned indefinite saving and investment by individuals *without regard* to the social conse-

^{*} Translation: Muhammad Asad, *The Message of the Qur'an*, Gibraltar: Dar al-Andalus, 1980.

⁸ Jacob Viner in his erudite evaluation of Weber's thesis has summarized what Weber called ascetic Protestant ethics: "... a dedicated and unlimited pursuit of wealth through unremitting industry, rigid limitation of expenditures on personal consumption or charity, concentration of time and attention on the pursuit of one's business affairs, avoidance of distraction through intimate friendship with others, systematic and pitiless exploitation of labour and strict observance of honesty in one's relations with others within the limits set by 'formal legality' " [8, p. 151]. See also Raymond Aron [2] for an evaluation of the Weberian thesis. Such glaringly irrational and unattractive behaviour could never have been condoned by Islam, which forbids all the prerequisites of capitalism described in the above pithy summation of Protestant ethics.

quence of such actions. Islam prohibits ostentatious personal consumption, but extols giving as a means of equalizing income distribution *and* of achieving spiritual bliss as well. Private property is a sacred trust, to be shared by all, particularly by the poor and the needy.⁹

It is important to note here that capitalism is an omnibus term which encompasses: (i) the capitalistic mode of production; (ii) the capitalistic socio-economic framework; and (iii) the capitalistic mentality. At a fundamental level, these are only three aspects of the same phenomenon. However, it is possible for one or two of these elements to be found in non-capitalistic systems as well. For instance, in so far as the capitalistic mode of production refers to a rising capital-intensity of the commodity-producing sectors (interpreting capital to include human capital as well), this is the characteristic of every growing economy. In fact, socialistic societies have carried this process to the extreme by over-emphasizing the establishment of heavy industries as a means of economic prosperity. *However, it should be noted that economic growth in an Islamic economy cannot be a pretext for exaggerating inequities in the distribution of income or for adding to human misery by imposing economic or political servitude on the common man.* It is an absolute rule that any policy that aggravates or even condones social injustice is un-Islamic simply because it violates the Equilibrium axiom.

The falsity of any reasoning that equates the Islamic system with capitalism (minus interest) on the basis of certain formal similarities – e.g. in the name of political freedom – will become transparent once the matter is looked at in terms of the Islamic ethical axioms. Firstly, capitalism fails to realize the unity of life by over-emphasizing, through the capitalistic mentality, man's material values at the cost of his spiritual aspirations. Indeed, the longing for material acquisitions dulls creative faculties in man and dries up the well-springs of happiness, which flow from creative work. According to the Islamic point of view, such an attitude is a fatal diversion of man's efforts, which should instead be bent to the realization of his theomorphic nature. "Who hath gathered wealth (of this world) and

⁹ The Islamic Ideal, as evidenced by the pious Muslims in the early years after the death of the Prophet Muhammad (Blessings of Allah and peace be upon him), had emphasized collective ownership, *not* State ownership, of the wealth of the Muslim community.

arranged it. He thinketh that his wealth will render him immortal. Nay, but verily he will be flung to the Consuming One" (104:2–4). Hence the acquisition of money has been reduced considerably in the scale of human values in the Islamic perspective. The Qur'ān makes this clear: "Wealth and children are an ornament of life of the world. But the good deeds which endure are better in thy Lord's sight for reward, and better in respect of hope" (18:47).

Secondly, capitalism destroys Nature's Equilibrium. It allows wealth to become concentrated in a few hands on the ground that only the rich save and invest. The institution of private property further sets up a vicious circle wherein opportunities for material advancement are pre-empted by the owners of wealth who draw the web of vested interest ever tighter to increase the distance between the haves and the have-nots.¹⁰ The failure of capitalism to keep social equilibrium also follows from its undue emphasis on competition – indeed, cut-throat competition – as a key to worldly success. By contrast, as pointed out above, the Holy Qur'ān rejects the closed circle of wealth getting narrower at each turn, admonishing that "it (i.e. wealth) become not a commodity between the rich among you" (59:7). According to Islam, life is a matter of mutual co-operation and personal responsibility. Though not altogether excluding competition, Islam does not recognize it to be the best way to attain human happiness or even as a guiding principle of economic behaviour. This is because, in a regime of socio-economic inequities that spoil the environment under capitalism, free competition aggravates social injustices instead of reducing them.

Thirdly, while capitalism formally espouses the cause of human freedom, particularly at the political level, this is not the type of freedom that the Islamic concept of Free Will enjoins. As pointed out in Chapter 2, Islam's is a specific type of economic freedom which is founded on the *fact* that all property belongs to God and that man holds it in trust for Him, pointing to the *collective* ownership of wealth. Hence, the unqualified support to the institution of private property on which capitalism rests finds no echo in Islamic thinking. All the more so, because an unlimited licence for private property leaves little room for human freedom by imposing very

¹⁰ The initial wealth differentials lead to income differentials as well. The possibility of lending money at a positive rate of interest plays a key role in this de-equalizing wealth-income chain. Islam prohibits interest (*ribā*) and severely restricts the right to private property to eliminate economic exploitation in all its forms.

light social responsibility on those who have at the expense of the have-nots.

Fourthly, capitalism does not emphasize collective responsibility in the same sense and to the same extent as Islam does. True, responsibility is forced on individuals through policies like progressive income taxes and death duties, yet the individual in such societies is almost entirely attuned to grabbing rather than giving. Widespread tax avoidance and tax evasion, hidden from the public eye in a labyrinth of complicated legal systems, attest to the insensitiveness of the individual to collective responsibility.¹¹ Islam spurns such irresponsible social behaviour.

Welfare State Doctrine

If Islam accepts neither socialism nor capitalism, then what is its attitude towards the welfare state doctrine, which seeks to strike a balance between these two systems.¹² In view of its heavy egalitarian bias, the Islamic system has often been compared with a welfare state on the ground that the basic social attitudes of the two systems are so similar that if one were constrained to choose from among the economic systems that already exist, then a welfare state would almost certainly be picked out by Muslim policy-makers as the next best economic institution. Like the welfare state, Islam enjoins upon its followers to achieve a "golden mean" in both their individual and social lives. In fact, the Muslim nation has been characterized in the Holy Qur'an as the "people of the middle" – "We have appointed

¹¹ In this respect, socialism does just the reverse of what capitalism practises: it over-emphasizes responsibility but destroys human freedom.

¹² The welfare state doctrine, not stated as such in the economics literature, is contained in several strands of European thought. In Britain Syndicalism tried to achieve a balance between the power of the State and individual freedom. It rejected both the unqualified support of capitalism to the institution of private property and the excessive collectivistic tendencies of socialism. However, it could not really get off to a start as a practical action programme. See Bertrand Russell [7]. In the Scandinavian countries, there has been a long tradition of combining individual freedom with social responsibility, by insisting on a socialistic economic programme along with political democracy. The results have been highly satisfactory, in terms of both a moderate economic growth and an egalitarian income distribution. However, due to the absence of appropriate ethical props, even this system is labouring under the crushing weight of moral turpitude. At a theoretical level, the doctrine gets support from welfare economics, first systematized by A. C. Pigou. This branch of economics, which has now reached a high level of sophistication (and abstraction) in the hands of economists like Oscar Lange, Graff, Little and Arrow, started off with a theory of State intervention in the presence of domestic distortions, like monopoly, externalities, etc., which result in "market failure" – market prices failing to conform to the "shadow prices".

you a middle nation . . ." (2:143) – that is a nation which avoids extremes.¹³ However, it should be noted that unlike the welfare state, *Islam is not the mean between socialism and capitalism*, but is symptomatic of a general philosophy which abhors unnatural extremist behaviour at individual and collective levels.

Fundamentally, the welfare state doctrine is based on the dictum: "From everyone according to his ability and to everyone according to his needs." What this rule does is to "separate" the individual's capacity to earn from the title of every individual in the society to a life-preserving minimum sustenance. To enforce the above-mentioned requirement, the welfare state doctrine stipulates the creation of institutions which ensure the satisfaction of two basic rules: (i) production should be expanded in various sectors of the economy in such a way as to equalize the marginal social productivity among them; and (ii) the distribution of income among all consumers must be such as to equalize their marginal utility of consumption. The system of free markets, as stipulated under capitalism, does not contain any built-in mechanisms guaranteeing the satisfaction of either of these two rules. Hence, state intervention becomes necessary to regulate production as well as consumption.¹⁴ The Islamic position in this respect is very much the same. The Islamic welfare dictum, which corresponds to the one noted above, is contained in the following Qur'anic verse: "And in their wealth the beggar and the destitute* had due share" (51:19).¹⁵ Clearly and explicitly the "separability" of consumption from the individual's capacity to earn has been laid down here. Islam stipulates to bridge this gap by a conscious redistributive policy, equalizing income and wealth marginally as well as intramarginally. In fact, Islam goes

¹³ Some English translators of the Holy Qur'an substitute "best" for "middle". This is yet another instance of the Islamic philosophy which considers the middle course to be the "best course", since it is the path to attain *al-'Adl*, i.e. Equilibrium.

¹⁴ The satisfaction of the first rule, according to the welfare economics, requires an appropriate tax-cum-subsidy policy to achieve the social optimum in production. However, the second rule requires for its satisfaction nothing less than the creation of government-sponsored institutions to effect an appropriate redistribution of income and wealth and to provide the sick, the old and the needy with a minimum level of consumption.

¹⁵ In Pickthall's translation, which we have uniformly used throughout this book, the word "outcast" appears instead of "destitute". However, according to most of the Islamic scholars, "destitute" is a better translation.

*Although Pickthall translated the Arabic word *al-mahroom* as "the destitute" in this *ayah*, the correct translation of the word according to authentic Arabic scholars is "the deprived" – i.e. those who have been injudiciously deprived of their rights and possessions. This may be kept in mind while reading the above translation elsewhere in the book.

much further along the egalitarian road. As will be pointed out in Chapter 6, it does not even recognize man's unlimited right to what he owns because all wealth belongs to Allah. Furthermore, by adding a spiritual dimension to socially desirable acts, Islam strengthens the operational effectiveness of egalitarian forces in the society.

While the similarities between the two systems are quite fundamental, no less basic are the dissimilarities which distinguish the one from the other.¹⁶ Firstly, like all non-Islamic social systems, the welfare state doctrine has not been erected on the unitary concept of life, which is original with Islam. This does not mean that it fails to recognize the essential connection between ethics and economics; only the overall perspective in which this equation is perceived is quite different from the Islamic point of view. Islam's originality lies in *making ethics the point of departure of its view on economics*. By contrast, the welfare state ethics, which are by and large secular, do not aim at a "vertical" integration of man's materialistic and spiritual aspirations. As noted in the previous chapter, such differences have a fundamental bearing not only on what individuals consider "rational" behaviour, but on the entire spectrum of economic activities – viz. consumption, production and distribution. Furthermore the "character" of the social welfare function also undergoes a profound change once Islam's distinctive unitary bias is explicitly built into it. By the same token, the quality of Equilibrium is not the same under the two systems. Equilibrium positions, defined differently under the Islamic system, will be characterized by a distinctive "consumption" basket, excluding those commodities the consumption of which has been banned in Islam. To provide for it, the production structure will also have to be oriented in a different fashion. These differences will remain even if, as is not unlikely, the distribution of income and wealth is similar under these two egalitarian economic systems, and even though both emphasize human freedom and responsibility.¹⁷

¹⁶ This is achieved mainly by a combination of a set of policies of substantially diluting the institution of private property, the abolition of interest and the introduction of *Zakāt* (i.e. the poor due).

¹⁷ As noted in Chapter 2, while both economic systems lay great store by human freedom and responsibility, these two terms do not carry the same connotation under these systems. Furthermore, the exact balance of these two elements is quite distinctive in Islam. The economic consequences of these differences have already been worked out in Chapter 3.

Summary

It should now be quite obvious why an Islamic economic system "exists", in the logical sense of being consistent and economically viable, side by side with, though apart from, the existing economic systems. While there are formal inter-system similarities, yet the unitary Islamic philosophy, with its emphasis on equilibrium, freedom and responsibility, sets it apart from every other system. Moral obligations both restrain and reinforce economic compulsions strictly according to the dictates of Islam's ethical philosophy. When the pursuit of economic welfare turns into the worship of money, Islam has nothing to do with such an immoral preoccupation. On the other hand, in so far as redistribution of income and wealth enhances material welfare, Islam adds a spiritual dimension to such an activity: "Ah, what will convey unto thee what the Ascent is! (It is) to free a slave, and to feed in the day of hunger; an orphan near of Kin, Or some poor wretch in misery." (90:12–16). Indeed, the peculiarities of this Divine Synthesis of ethics and economics "condition" profoundly the interrelationship among consumption, production and distribution in an Islamic economic system and set it apart from all other economic systems. Once this central feature of Islamic economics is clearly grasped, there is no possibility of confusing it with capitalism, socialism or the welfare state. Regulation of the economic life by the State will be quite considerable in an Islamic economy. However, unlike socialistic societies, Islam has nothing authoritarian in its attitude towards economic processes; for no totalitarian nightmares haunt an Islamic economy. State intervention directed primarily at reconciling the possible social conflicts between man's ethical and economic behaviours cannot lead the society onto the "road to serfdom" but will guide it gently along the road to human freedom and dignity. Nor is moral degradation allowed in the name of economic prosperity and unrestrained human freedom. The middle-of-the road economic philosophy of Islam steers clear of undue extremism in human behaviour.

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CHAPTER I

The Basic Policy Objectives

PART III

THE ANATOMY OF AN ISLAMIC ECONOMY

"Say: My Lord enjoineth justice"
The Holy Qur'ān (7:29).

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PART III

THE ANATOMY OF AN ISLAMIC ECONOMY

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The Basic Policy Objectives

The last two chapters have dealt with the general principles of an Islamic economic system with a view to substantiating its claim to originality. It has been shown that ideologically the Islamic economic system stands prominently on its own, clearly distinguishable from all existing economic systems. Its distinction derives from Islam's original ethical conception, which determines the character of everything else that follows. Having shown that an Islamic economy "exists" in the logical sense, our next step is to delineate clearly guidelines for the policy-makers in such a social milieu with respect to the basic set of policy objectives that they should be pursuing in search of the Islamic ideal.

How does one go about identifying an Islamically-legitimate set of objectives? As pointed out in the preceding chapters, the primary preoccupation of the policy-makers in an Islamic society should be to provide for an explicit mechanism to re-establish Equilibrium, in the specific Islamic sense, and maintain it over the course of time. In particular, it will be essential to close the interclass cleavage by moving all social classes towards a golden mean in terms of an acceptable living standard: the poor will have to be moved up, and the rich pushed down to this common social denominator. This is by no means an easy undertaking. To succeed, broad social priorities of an Islamic economy will have to be clearly defined and a conscious redirection of real and financial resources effected accordingly. It is shown in this chapter that in an Islamic economic system, these priorities translate into four objectives: social justice, universal education, "optimal" rate of economic growth and the maximization of employment generation.

It may be argued that there is nothing new or distinctive about these objectives since they are common to all economic systems. One may ask if, with these common objectives, the Islamic economic system, in terms of the quality of life that it promotes, would not be similar to other economic systems. The answer is in the negative

because the pursuit of these objectives in an Islamic economic system must be guided and constrained by Islam's own ethical philosophy. That should make all the difference in the world. For example, as noted below, the very concept of social justice has a distinctive connotation in an Islamic society. Furthermore, once the requirements of social justice are specified and resources allocated optimally to meet them, a distinctive growth path satisfying the Islamic ethical constraints will also be differently determined.

Social Justice

Social justice, an aspect of the universal law of Equilibrium, forms the cornerstone of the Islamic economic system: "Say: My Lord enjoineth justice" (7:29).¹ It implies guarantees for individual freedom against any misuse of power – economic, political or physical – by those who possess it. It also saddles all sections of the society with the responsibility that goes with freedom. Social justice is not only economic justice: it also requires a simultaneous and *proportionate* – that is proportionate to the social structure – adjustment of power in all aspects of human life, which, in the Islamic perspective, forms an irreducible Unity. There can be no justice if all are not equal before the law since all are equal before God. Hence the exhortation for being absolutely even-handed in the dispensation of justice: "Be ye staunch in justice, witnesses for Allah, even though it be against yourselves or (your) parents or (your) kindred, whether (the case be of) a rich man or a poor man, for Allah is nearer unto both (than ye are)" (4:135). Social justice to succeed must also be translated in man's day-to-day behaviour, which should be free of trivialities and cantankerousness: "... let not hatred of any people seduce you that ye deal not justly" (5:8). The quality of justice must shine through man's conduct of his day-to-day mundane affairs. Hence people should be neither defrauded nor deprived of what

¹ It is interesting to note that the word "justice" is the third most-used word in the Holy Qur'ān and has been repeated more than a thousand times. (The other two words are "Allah" and "knowledge", in that order). However, it should be noted here that in the Qur'ānic perspective "justice" must be tempered with "compassion" to avoid unnecessary social hardships: "Lo! Allah enjoineth justice and kindness [*al-'Adl wa al-Ihsān*]" (16:90). On the social plane, the requirement of *al-Ihsān* will generally reinforce the process of securing *al-'Adl*, because social justice requires the poor to be moved up and the rich to be moved down the scale of social hierarchy.

properly belongs to them: "Give full measure and full weight in justice, and wrong not people in respect of their goods" (11:85). Furthermore, gross inequalities in income and wealth are not consistent with the Islamic ideal because they essentially reflect the unjust character of the society. For in the Islamic perspective, "it (i.e. wealth) become not a commodity between the rich among you" (59:7). In fact, it *cannot* circulate among the rich because "in their wealth the beggar and the destitute had due share" (51:19). It follows that any institutional impediments to the attainment of the Equilibrium level of wealth must be removed through effective redistributive policies.

Four basic points must be noted about Islam's distinctive conception of social justice. Firstly, the Islamic point of view on social justice is based on the principle that all that exists in the Universe belongs to God: "Allah's is the heritage of the heavens and the earth" (3:180). Man, because of his being God's vicegerent on earth and by virtue of his theomorphic character, has been granted the ownership of His bounties: "Hast thou not seen how Allah hath made all that is in the earth subservient unto you?" (22:65). However, this title is not unrestricted; for man holds it only in trust. *He must, therefore, dispose of it as a trustee, not as an absolute owner.* It also follows that if man does not perform all his duties voluntarily – something that seldom happens – then institutions must be created to bring man's individual behaviour in line with the community's collective behaviour. He can neither hoard wealth, of which he is merely a trustee, all for his own person: "That which they hoard will be their collar on the Day of Resurrection" (3:180); nor can he squander it away with unrestrained abandon: "Squander not your wealth among yourselves in vanity . . ." (4:29). Voluntary giving by the rich to the poor forms the bridge between hoarding and squandering, both of which will be minimized once income and wealth are distributed equitably.

Secondly, while insisting on a powerful built-in income-redistributive mechanism, made even more powerful by its alignment with God's pleasure, Islam does allow some income inequality *on the margin* to promote individual initiative. In particular, differences in earnings resulting from unequal innate intellectual endowments are allowed for: "He it is Who hath placed you as viceroys of the earth and hath exalted some of you in rank above others, that He may try you by (the test of) that which He hath given

you" (6:166). However, even here Islam does not lose sight of the fact that these differences may have been due, as is usually the case, to unequal opportunities, deriving mainly from the institution of private property. *In the Islamic perspective, "initial" impediments to income equalization must first be removed before even the marginal income inequalities can be justified.* (See Chapter 9 *infra*.)

Thirdly, social justice in Islam is rooted in man's faith. Indeed, man's belief in God entails an automatic duty to do justice. The one cannot exist without the other: "Those who believe and obscure not their belief by wrong-doing, theirs is safety; and they are rightly guided" (6:83). Income redistribution, induced through voluntary giving, along with the compulsory resource transfers effected through *Zakāt* and State taxes, is not only an economic necessity but also a means to spiritual salvation: "Take alms of their wealth, wherewith thou mayst purify them and mayst make them grow, and pray for them" (9:103). Hence, according to the distinctive Islamic conception of social justice, economics become effectively integrated with ethics to help realize the Unity of life. Furthermore, in so far as giving is a symbol of man's responsibility to the society, it has been made obligatory: "Establish worship and pay the poor-due and obey the messenger . . ." (24:56). By the same token, this system preserves human freedom by delivering man from poverty, want and moral degradation.

There is no complacency that the powerful vested interests in the society will not obstruct the Islamically ordained income-equalization processes. If they do, even violence can be resorted to for breaking the hold of this parasitic class. True, Islam's general preference is to avoid social upheavals. However, this preference for non-violence comes into play only when socially just conditions have already been established: "Work no confusion in the earth after the fair ordering (thereof) . . ." (7:56). This is not a plea of some kind of reactionary *status quoism*, but a warning to inveterate wrong-doers whose habit it is to disturb social order, just or unjust. The quality of Equilibrium (*al-'Adl*) is absolute in Islam and must be preserved in all of man's multifarious activities.

Fourthly, at the philosophical level, the Islamic concept of social justice rests on its view about what maximizes human happiness. In the Islamic perception, human happiness rests on man's knowledge of the Absolute: "Lo! the righteous will dwell among gardens and rivers, firmly established in the favour of a Mighty King"

(55:54–55). On the plane of social existence, *this knowledge gets translated into good acts, which have been specified in advance*: "Who hath created life and death that He may try you, which of you is best in conduct" (67:2). Human happiness is enhanced in proportion to the accomplishment of such acts. It may be interesting to note that this view of human happiness is exactly the reverse of the Benthamite philosophy of Maximum Happiness, according to which an act is good if it maximizes happiness, which is pursued by individuals on their own.² In other words, happiness is whatever makes man happy. Translated into an operational principle, such "relativism" can lead only to social anarchy. Bentham was aware of this problem, and sought to resolve it by proposing to regulate the individualistic, selfish pursuit of happiness in order to reconcile it with public interest. However, this prescription sends us back to square one: we are now asked to define (or redefine) what it is that constitutes a *legitimate* pursuit of happiness. This problem can be solved by cataloguing the permissible objects of happiness, which is basically a non-terminating process.

A simpler and a more realistic approach – one which can readily be made operational – is to specify instead the acts by reference to which human happiness can be "measured". This is exactly the Islamic prescription for human happiness, which comes not so much from the possession of material goods as from contentment and gratitude.³ "Wealth and children are an ornament of life of the world. But the good deeds which endure are better in thy Lord's sight for reward, and better in respect of hope" (18:47). Such an approach has an aura of universality around it. All nations since time immemorial have been led, by conscience and good reason, to frame rules of good behaviour. Islam approves of them all: "Thus unto every nation have We made their deed seem fair" (6:109). But exactly what these fair deeds are has also been specified: "Each one doth according to his rule of conduct, and thy Lord is best aware of him whose way is right" (17:84). True, there is an air of absolutism about this concept of human happiness; but this is exactly what gives

² For a brief account of the Benthamite ideas, see Bertrand Russell [3]. The latter-day *laissez faire* philosophy of Adam Smith was based on the Maximum Happiness doctrine.

³ Once again, the Islamic posture runs counter to the Benthamite principle, which does not "grade" happiness: "quantity of pleasure being equal, pushpin is as good as poetry". Islam rejects such attitudes precisely because the quantity of pleasure derivable from different actions is *not* equal, the difference being attributable to the ethical contents of each.

it a perspective of certitude and equilibrium, a combination without which a state of bliss cannot endure even if it is accidentally attained.⁴

Universal Education

Man is theomorphic in nature; but to actualize this God-given potentiality the acquisition of knowledge has been made obligatory. In fact, man's title to superiority over all creation is based on his superior knowledge: "And He taught Adam all the names, then showed them to the angels, saying: Inform me of the names of these, if ye are truthful" (2:31). Hence, Islam, instead of equalizing the ignorant and the knowledgeable, differentiates between them: "Allah will exalt those who believe among you, and those who have knowledge, to high ranks" (58:11). Even more pointedly: "Say (unto them, O Muhammad): Are those who know equal with those who know not? But only men of understanding will pay heed" (39:9). It is for this reason that man has been advised to pray constantly: "My Lord! increase me in knowledge" (20:114).⁵ The acquisition of knowledge is the best way not only to worldly good but also to spiritual glory: "He giveth wisdom unto whom He will, and he unto whom wisdom is given, he truly hath received abundant good. But none remember except men of understanding" (2:269). In fact, knowledge is useful *only* if it unifies mundane activities with the possibilities of spiritual ascension – thus whosoever, the individual or the State, promotes or accelerates the process of the acquisition of useful knowledge in fact participates in God's plan.

It clearly follows that an Islamic society must distinguish itself by the quality and excellence of its educated class. Furthermore, since all men are theomorphic, every meritorious child, irrespective of the accident of his birth, must receive an equal opportunity to fructify this faculty. Hence an explicit provision for *universal education* becomes one of the primary objectives of an Islamic society. This process has to be subsidized (and in due course made completely free

⁴ In the language of mathematics, the qualities of certitude and equilibrium act as "stability conditions" in social dynamics, bringing the society back to the straight path of Islam.

⁵ After "Allah", the word "knowledge" is the second most-repeated word in the Holy Qur'an.

of charge) through a conscious programme of action. Such a policy will be essential to establish social justice over a period of time because, starting from a position where men are differently endowed with wealth and property, education has a great equalizing effect on income distribution. In this way, education helps restore Equilibrium. It guarantees human freedom, and brings up the type of people who not only know the worth of their freedom but are also prepared to take up the corresponding social responsibility. However, it must be noted that the fruits of education cannot be distributed equitably without far-reaching socio-economic reform aimed at securing social justice. In particular, the "initial" differentials of wealth are an important determinant of the potential recipients of education and the quality of their attitudinal response as members of the society.⁶ Thus the extent to which education promotes Equilibrium will depend crucially on the success of the wider socio-economic effort at ushering in a balanced and homogeneous society, rid of exploitative vested groups.⁷

Economic Growth

The quality of Equilibrium holds not only at a given point in time but through time as well. Hence, in the Islamic perspective, economic growth is a means of ensuring social justice inter-temporally.⁸ Islam does not permit the present generation to be excessively myopic in its views about social justice. For social justice according to Islam is an essential element of social dynamics; it is not a prescription for economic stagnation. It is in the context of a growing economy that the national income "pie" can be enlarged to allow each recipient not only an increase in his relative share but also

⁶ Bertrand Russell noted: "Whenever class distinctions exist, education necessarily has two correlative defects: that of producing arrogance in the rich and that of aiming at irrational humility in the poor" [2, p. 86]. Obviously both these attitudes, an integral part of the educational system in capitalistic societies, are highly undesirable and, therefore, contrary to the humane and rationalistic spirit of Islam.

⁷ In fact, by making belief in the Day of Judgement an integral part of his faith, man's vision has been extended to infinity, destroying, at the very source, selfishness that arises from an excessive obsession with what *is*.

⁸ It may be noted that in an Islamic economy (i.e. inter-temporal social justice), economic growth as an Islamically-legitimate policy objective does not need any independent demonstration (with reference to the Holy Qur'an and the *Sunnah*), since it has been defined as nothing but an intertemporal dimension of social justice.

in the absolute share in the pie. A social milieu wherein everybody gains in absolute terms, with the poor even getting a higher relative share, is clearly superior to the one in which one can gain only at the expense of others.

Thus, growth policy in an Islamic economy should aim at equalizing, on the margin, the competing claims of present and future consumption. In technical parlance, the policy-maker must maximize an integral (i.e. the sum) of the utility of the flows of consumption over a specified period of time, subject to the constraint of providing enough resources for capital formation. However, in an Islamic society, the "argument" (i.e. the element) of the functional⁹ will be extended to include not only material welfare but spiritual bliss as well. The inclusion in the function of a term representing spiritual satisfaction should cause no mathematical problems because of its intangible character. For what is optimized, even according to neo-classical growth economics, is not the flow of consumption but the associated *utility*, which is itself an intangible quantity.¹⁰ And the magnitude of the flow of utility will be different precisely because, in view of the binding "allowability" constraints, the contents of the consumption basket will change substantially in an Islamic economy. Furthermore, the capital-formation constraint, noted above, will include explicitly human-capital as well as material capital. Indeed, there will be a greater emphasis on human capital formation for the simple reason that, in the Islamic perspective, man is the centre of all economic activity. This consideration should influence the composition of investment because the expenditure on education will now be considered an investment.

All these considerations add up to a growth path which is qualitatively different from the growth paths of all other economic systems, in terms of its consumption, production and distribution

⁹ See S. Chakravarty [1, esp. Chapter 2]. A "functional" – in which each of the terms in the argument is itself a function of time – that seeks to optimize the utility of consumption rather than the level of consumption is also preferred due to its mathematical and economic properties, e.g. the diminishing marginal utility of consumption. The difference between optimizing with respect to the flow of consumption and its utility is important since the units of consumption are not the same as the units of satisfaction.

¹⁰ Another point to be noted is that Islam extends man's time horizon up to, and beyond, the Day of Judgement. This consideration alone modifies the flow and composition of the consumption goods demanded in an Islamic society. Mathematically, however, this consideration should pose no problems since in this case time is equated to infinity, which is the standard format of a functional with an infinite time horizon.

"contents". Accordingly, *the very concept of growth in an Islamic economy will change in that it will be more comprehensive, including moral, spiritual and material aspects of man's life.* It follows that a "helter-skelter" growth, bought at a very high price in terms of the sacrifice of human happiness and spiritual values, falls right outside the unitary scheme of things envisaged in Islam. All the more so because such a strategy violates the axioms of Equilibrium, Free Will and Responsibility. Once this point is understood, it should be easy to see why maximizing the growth rate of national income *per se*, irrespective of its effects on income distribution and general welfare, cannot be the primary objective of an Islamic economy. In the parlance of economics, what an Islamic society will be aiming at is "optimal" growth – optimality being defined in the exclusive Islamic sense of also including spiritual welfare – with neither too little nor too much saving in the "initial" period. For Islam would accept neither capital consumption, leading to negative long-run growth, nor excessive growth which imposes unnatural sacrifices on the present generation. The quality of the long-run, inter-generational Equilibrium will be the guiding principle of an Islamic economy.

Looking back into history, Islam would have rejected the (1776) Industrial Revolution type of model as well as the communistic model of development (1917). Both these models have in common an excessive preoccupation with capital accumulation, continuously accelerated to ensure very high growth rates, on the premise that the higher the growth rate is the better it is for the society.¹¹ In both cases, the human cost of economic growth was cruelly excessive. Sharply contrasting income distribution creates social tensions; in fact, in extreme cases, it has led to full-scale social revolutions. This is because such a strategy in effect curtails human freedom in general, while setting at liberty a small but powerful section of the society. Under *laissez faire* capitalism, this class is represented by the capitalists, while it is symbolized by the ruling élite in the communist societies. Consciously or unconsciously, these models have been uncritically accepted by the planners in the developing

¹¹ In sharp contrast, the welfare states of Western Europe have followed a more moderate course of action, settling for modest growth rates, accompanied (in fact, constrained) by an egalitarian distribution.

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countries as the basic sources of inspiration.¹² However, precisely because it is inherently suboptimal, economically as well as morally, such a strategy back-fired in most of the countries (Pakistan included) where it was pursued. This is because, while high growth rates may be desirable (provided, of course, that they can be sustained), the resulting pattern of resource allocation may deviate sharply from the one implied by a growth rate which is optimal from the point of a socially desirable distribution of income. Thus a lower growth rate with better income distribution may turn out to be superior to a higher growth rate with a more contrasting distribution of income.

Maximizing Employment Generation

It should be obvious that an Islamic economy, in its quest for social justice, must ensure that economic growth makes a "maximum" contribution to the creation of new employment opportunities. However, it must be noted that the objective in an Islamic society is not to increase employment (i.e. to attain full employment) at the cost of economic efficiency. Generally speaking, additional employment must, in the long run, be generated in a *technically efficient* fashion, although in periods of economic depression employment may have to be created by a public works programme in order to alleviate immediate human misery. It is here that employment and education tie up with each other. Technically-feasible employment generation is determined ultimately by the average capital/labour ratio implicit in a specific growth path. An economy, like Pakistan's, which is short on capital and abundant in labour must find a technically efficient way of lowering the capital/labour ratio, so that higher growth entails higher employment.¹³ This can be

¹² The uncritical acceptance of the Harrod-Domar type models, with their exclusive emphasis on the degree of capital intensity as a primary determinant of economic growth, has also contributed to this state of affairs. The more operational models of Feldstein and Mahalanobis, emphasizing investment in heavy industries, only served to enhance the planner's obsession with increasing the degree of capital intensity as the key factor in accelerating the growth rate. This growth strategy has failed in all the labour-surplus economies leading to some kind of an "immiserizing growth": higher growth rates associated with increasing unemployment rates.

¹³ This is because economic growth, with no technological change, implies a rise in capital intensity. Hence, to generate more employment, while keeping the growth

achieved through technological progress focused on evolving a suitable technology in line with resource endowment. However, no technological breakthrough can be achieved in countries with very low literacy rates. By the same token, education will have to be geared largely to the acquisition of technical and scientific knowledge.

The argument that in an Islamic society higher employment should be generated mainly by lowering the capital/labour ratio is supported by the requirement of paying a "just" wage to the workers. While it cannot be defined in abstract terms, it is clear that the requirement of maintaining Equilibrium specifies (in broad qualitative terms) both the upper and the lower bounds of the level of a just wage: the market wage will not be "exploitative" on *either* side of the market. Neither the greed of the employers nor the extortionist trade unions will be allowed to dictate its level. However, this is not to say that both these influences will be absent from an Islamic economy: but only to point out that the State will have to play a crucial role in the determination of wages by reconciling the conflicting interests of the employers and the employees. However, one thing is clear: the "optimal" wage in an Islamic economy will not be low enough to maximize employment generation if the capital/labour ratios are not sufficiently lowered through technological change. Hence, it is only through this strategy that the Islamic economy can be prevented from getting trapped in what Kahn called "The Bastard Golden Age", according to which high growth is consistent with rising unemployment.

Summary

Social justice, universal education, economic growth and maximum employment are the basic policy objectives of an Islamic economy. Social justice requires an elimination of uneconomic and immoral inequalities in income and wealth. This process will be greatly strengthened by the creation of new employment opportunities in the lower income groups. Furthermore, there is the absolute necessity of universal education, which, in general, will determine the *quality* of social justice. However, social justice must

Footnote 13 continued

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laid down. Difficulties arise because, at least in the initial period of the Islamization process, the "first-best" solutions – i.e. those which satisfy *all* the ethical axioms – may simply not be available.³ As a result, the policy-maker may be constrained to choose from the "second-best" alternatives – i.e. those which satisfy some but not all of the ethical axioms.

Subject to these considerations, the problem of the choice of appropriate policy instruments has first been discussed at a general level in this chapter, while specific policies, like the problem of the abolition of a positive rate of interest in an Islamic economy, will be discussed in the next two chapters.

Broad Policy Issues

Since the quality of the Islamic system will be determined primarily by its success in bringing about social justice in all the aspects of man's life, it is essential that appropriate economic policies be adopted to achieve this goal in the shortest period of time. In this connection, there are two broad areas – viz. the institution of private property, and the legitimacy of socialization of the means of production – on which the Islamic point of view must be ascertained before an appropriate policy package suitable to an Islamic economy can be identified. Furthermore, since social justice must hold intertemporally as well, the qualitative aspects of economic growth assume special importance in an Islamic economy.

1) Institution of Private Property

To satisfy the requirements of social justice it is essential to adopt policies with a view to correcting excessive income inequalities not only on the margin but also intramarginally, i.e. those arising from an initial unequal wealth endowment. True, some, though not all, income inequalities are legitimate, e.g. those which arise from

³ The consequences of the obvious fact that establishing an Islamic economic system is not a one-shot affair, and hence a transition period must elapse before the final goal is accomplished, have not been fully worked out in the existing literature on Islamic economics. *The necessity of the first-best choice in a fully-fledged Islamic economy has often been confused with its economic and even ethical viability during the transition period.* These matters have been discussed in Chapter 9.

differences in the quality (and quantity) of labour input, so that the corresponding right of an individual to hold his money earnings in the form of a house or a piece of cultivable land should also be unexceptionable. However, serious moral and social problems arise when it comes to the right of an individual to hold property, in particular landed property, which is not due to his own labour and which he does not cultivate himself.

The general Islamic attitude on the matter is: "... man hath only that for which he maketh effort" (53:39). At the same time, the Islamic law of inheritance confers formal legitimacy on whatever wealth there is to inherit. What do these seemingly contradictory positions add up to? Does it follow that Islam provides a blanket approval to the institution of private property so long as it has been inherited in an Islamically-legitimate way? While it is not possible to provide definitive answers to such questions, there are a few basic considerations which may indicate a negative answer. Firstly, while Islam assigns a central position to the individual man, as a basic entity in his own right, by virtue of his God-given freedom, this freedom must be circumscribed, *a la* Responsibility axiom, to highlight the importance of his links with the society. It follows that in an Islamic economy the individual's right to private property cannot be unlimited simply because it can be sustained only by depriving others of their rights. This observation is strengthened by the fact that an unlimited property right also violates the absolute law of Equilibrium. At any rate, since economic initiative in an Islamic economy must be constrained by ethical considerations, voluntarily or through State action, the desire for material acquisition can never degenerate into the worship of money. Hence, the *demand* for private property cannot be "unlimited" (i.e. excessive by the prevalent social standards) in a fully-fledged Islamic economy.

As pointed out several times in earlier chapters, the individual man's unlimited natural right to private property, held sacrosanct under capitalism, has not been recognized by Islam.⁴ Man is not the absolute master of his property: "Unto Allah (belongeth) whatsoever is in the heavens and whatsoever is in the earth" (2:284), because "His is the Sovereignty of the heavens and the earth" (57:5). Man holds the right to property only as a trust: "and spend of that

⁴ It may be noted that, according to Islamic law, certain natural resources cannot be owned privately because they belong to the entire *Ummah* (i.e. the Muslim community).

be maintained not only at a given point of time but dynamically as well. This defines quite precisely the economic growth objective in an Islamic economy. The Islamic point of view on growth is conditioned by two closely-related considerations: (i) the general Islamic requirement to ensure a fair distribution of income and wealth *now* sets an upper bound on feasible growth rates; and (ii) the need to maintain intergenerational equity puts an upper limit on the magnitude of the resources which can be distributed now. Hence, enough resources must be spared from present use for capital formation. However, capital formation in an Islamic economy will have to explicitly include human capital formation, thereby accentuating the emphasis on education, which will now be counted as investment. Universal free education will help man to actualize his God-given potential: under appropriate conditions, education will set in motion an income-equalizing mechanism of great force. That some such approach is required to satisfy the dictates of social justice should be obvious if it is remembered that for a vast majority of the population, being employed is the only way to earn income. True, the unemployed will get paid from social security funds, but this is not enough because employment is not only a source of income but a title to self-respect, which Islam seeks to inculcate among all Muslims. Furthermore, a rising social security bill will have to be financed through additional taxation. Obviously, a better approach would be to finance additional education in order to ultimately enhance employment opportunities. The essential point to grasp is that the overriding quality of an Islamic economy is Equilibrium, which must be re-established in a systematic, conscious and economically viable fashion to ensure that unity of life remains intact, and human freedom unimpaired, constrained only by the social responsibility to realize the Islamic ideal for a just and dynamic social order.

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Choice of Policy Instruments: General Issues

This chapter indicates broad guidelines of the problem of the choice of policy instruments in an Islamic economy. This is a more difficult task than specifying the policy objectives because of the two peculiarities of an Islamic economy. Firstly, as a general rule, Islam insists not only on the legitimacy of the policy goals, but also on the policy instruments, which must satisfy, or at least be not inconsistent with, the fundamental ethical axioms of Islam, to ensure that the pursuit of the Islamic ideal has a common focus.¹ At the same time, it also restricts the Islamically legitimate set of policy instruments, which will be smaller — e.g. a positive rate of interest will no longer be in the set — than the one available under non-Islamic economic systems. This restriction will complicate policy-making because the taxonomic equation between policy objectives and policy instruments may no longer be satisfied.² If so, the Muslim policy-makers will have to find new policy instruments to replace the ones discarded.

Secondly, the task of replacing one policy instrument with another is by no means a mechanical one. In the Islamic perspective, while human discretion has been constrained with respect to what cannot be done, no such binding specifications have been prescribed about what can or should be done instead. Only the broad ethical requirement — namely conformity with the ethical axioms — has been

¹ However, while this principle holds generally, Islamic realism leaves room for exceptions when "ends may sanctify the means"; also, in appropriate circumstances, "means may profane the ends". Indeed, these exceptions are also a part of the divinely revealed vision of Islam, and just one example of Islam's ethical philosophy: it never pulls in the web of individual idealism so tightly as to exclude collective possibilities. See Frithjof Schuon [8, p. 28]. An example of ends sanctifying the means is the use of force to make recalcitrant souls see the truth. This is the philosophy behind *Jihād* (i.e. the war against *all* evil), which is one of the basic cornerstones of Islamic teaching.

² It is a well-known principle in economics that in a general-equilibrium framework policy instruments must be proportional (in fact, equal) to the policy objectives. See, for instance, Jan Tinbergen [9] and James Meade [5]. This is called the "taxonomic" approach.

be maintained not only at a given point of time but dynamically as well. This defines quite precisely the economic growth objective in an Islamic economy. The Islamic point of view on growth is conditioned by two closely-related considerations: (i) the general Islamic requirement to ensure a fair distribution of income and wealth *now* sets an upper bound on feasible growth rates; and (ii) the need to maintain intergenerational equity puts an upper limit on the magnitude of the resources which can be distributed now. Hence, enough resources must be spared from present use for capital formation. However, capital formation in an Islamic economy will have to explicitly include human capital formation, thereby accentuating the emphasis on education, which will now be counted as investment. Universal free education will help man to actualize his God-given potential: under appropriate conditions, education will set in motion an income-equalizing mechanism of great force. That some such approach is required to satisfy the dictates of social justice should be obvious if it is remembered that for a vast majority of the population, being employed is the only way to earn income. True, the unemployed will get paid from social security funds, but this is not enough because employment is not only a source of income but a title to self-respect, which Islam seeks to inculcate among all Muslims. Furthermore, a rising social security bill will have to be financed through additional taxation. Obviously, a better approach would be to finance additional education in order to ultimately enhance employment opportunities. The essential point to grasp is that the overriding quality of an Islamic economy is Equilibrium, which must be re-established in a systematic, conscious and economically viable fashion to ensure that unity of life remains intact, and human freedom unimpaired, constrained only by the social responsibility to realize the Islamic ideal for a just and dynamic social order.

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Choice of Policy Instruments: General Issues

This chapter indicates broad guidelines of the problem of the choice of policy instruments in an Islamic economy. This is a more difficult task than specifying the policy objectives because of the two peculiarities of an Islamic economy. Firstly, as a general rule, Islam insists not only on the legitimacy of the policy goals, but also on the policy instruments, which must satisfy, or at least be not inconsistent with, the fundamental ethical axioms of Islam, to ensure that the pursuit of the Islamic ideal has a common focus.¹ At the same time, it also restricts the Islamically legitimate set of policy instruments, which will be smaller – e.g. a positive rate of interest will no longer be in the set – than the one available under non-Islamic economic systems. This restriction will complicate policy-making because the taxonomic equation between policy objectives and policy instruments may no longer be satisfied.² If so, the Muslim policy-makers will have to find new policy instruments to replace the ones discarded.

Secondly, the task of replacing one policy instrument with another is by no means a mechanical one. In the Islamic perspective, while human discretion has been constrained with respect to what cannot be done, no such binding specifications have been prescribed about what can or should be done instead. Only the broad ethical requirement – namely conformity with the ethical axioms – has been

¹ However, while this principle holds generally, Islamic realism leaves room for exceptions when “ends may sanctify the means”; also, in appropriate circumstances, “means may profane the ends”. Indeed, these exceptions are also a part of the divinely revealed vision of Islam, and just one example of Islam’s ethical philosophy: it never pulls in the web of individual idealism so tightly as to exclude collective possibilities. See Frithjof Schuon [8, p. 28]. An example of ends sanctifying the means is the use of force to make recalcitrant souls see the truth. This is the philosophy behind *Jihād* (i.e. the war against *all* evil), which is one of the basic cornerstones of Islamic teaching.

² It is a well-known principle in economics that in a general-equilibrium framework policy instruments must be proportional (in fact, equal) to the policy objectives. See, for instance, Jan Tinbergen [9] and James Meade [5]. This is called the “taxonomic” approach.

laid down. Difficulties arise because, at least in the initial period of the Islamization process, the "first-best" solutions – i.e. those which satisfy *all* the ethical axioms – may simply not be available.³ As a result, the policy-maker may be constrained to choose from the "second-best" alternatives – i.e. those which satisfy some but not all of the ethical axioms.

Subject to these considerations, the problem of the choice of appropriate policy instruments has first been discussed at a general level in this chapter, while specific policies, like the problem of the abolition of a positive rate of interest in an Islamic economy, will be discussed in the next two chapters.

Broad Policy Issues

Since the quality of the Islamic system will be determined primarily by its success in bringing about social justice in all the aspects of man's life, it is essential that appropriate economic policies be adopted to achieve this goal in the shortest period of time. In this connection, there are two broad areas – viz. the institution of private property, and the legitimacy of socialization of the means of production – on which the Islamic point of view must be ascertained before an appropriate policy package suitable to an Islamic economy can be identified. Furthermore, since social justice must hold intertemporally as well, the qualitative aspects of economic growth assume special importance in an Islamic economy.

(i) Institution of Private Property

To satisfy the requirements of social justice it is essential to adopt policies with a view to correcting excessive income inequalities not only on the margin but also intramarginally, i.e. those arising from an initial unequal wealth endowment. True, some, though not all, income inequalities are legitimate, e.g. those which arise from

³ The consequences of the obvious fact that establishing an Islamic economic system is not a one-shot affair, and hence a transition period must elapse before the final goal is accomplished, have not been fully worked out in the existing literature on Islamic economics. *The necessity of the first-best choice in a fully-fledged Islamic economy has often been confused with its economic and even ethical viability during the transition period.* These matters have been discussed in Chapter 9.

differences in the quality (and quantity) of labour input, so that the corresponding right of an individual to hold his money earnings in the form of a house or a piece of cultivable land should also be unexceptionable. However, serious moral and social problems arise when it comes to the right of an individual to hold property, in particular landed property, which is not due to his own labour and which he does not cultivate himself.

The general Islamic attitude on the matter is: "... man hath only that for which he maketh effort" (53:39). At the same time, the Islamic law of inheritance confers formal legitimacy on whatever wealth there is to inherit. What do these seemingly contradictory positions add up to? Does it follow that Islam provides a blanket approval to the institution of private property so long as it has been inherited in an Islamically-legitimate way? While it is not possible to provide definitive answers to such questions, there are a few basic considerations which may indicate a negative answer. Firstly, while Islam assigns a central position to the individual man, as a basic entity in his own right, by virtue of his God-given freedom, this freedom must be circumscribed, *a la* Responsibility axiom, to highlight the importance of his links with the society. It follows that in an Islamic economy the individual's right to private property cannot be unlimited simply because it can be sustained only by depriving others of their rights. This observation is strengthened by the fact that an unlimited property right also violates the absolute law of Equilibrium. At any rate, since economic initiative in an Islamic economy must be constrained by ethical considerations, voluntarily or through State action, the desire for material acquisition can never degenerate into the worship of money. Hence, the *demand* for private property cannot be "unlimited" (i.e. excessive by the prevalent social standards) in a fully-fledged Islamic economy.

As pointed out several times in earlier chapters, the individual man's unlimited natural right to private property, held sacrosanct under capitalism, has not been recognized by Islam.⁴ Man is not the absolute master of his property: "Unto Allah (belongeth) whatsoever is in the heavens and whatsoever is in the earth" (2:284), because "His is the Sovereignty of the heavens and the earth" (57:5). Man holds the right to property only as a trust: "and spend of that

⁴ It may be noted that, according to Islamic law, certain natural resources cannot be owned privately because they belong to the entire *Ummah* (i.e. the Muslim community).

whereof He hath made you trustees" (57:7). It is for this reason that man is advised not to hoard his wealth for posterity: "And spend of that wherewith We have provided you *before death cometh* . . ." (63:10) (italics supplied); and "Let him who hath abundance spend of his abundance" (66:7). If through a combination of voluntary individual action and legislative steps these commandments are turned, as they must be, into operational rules of social behaviour, the amount of inheritable wealth would be severely limited. It follows that the total *supply* of private property – i.e. the inheritable wealth – should be much smaller in an Islamic society than in a capitalistic society.

Thirdly, between the limited supply of and the demand for private property, whatever little remains of inheritable wealth will be effectively diffused through the law of inheritance, the strict observance of which is obligatory not only on the present owners but also on future recipients.

It follows that, in view of Islam's predominant emphasis on social justice, *a la* Equilibrium axiom, the law of inheritance cannot be interpreted as the preserver of any anachronistic and oppressive social system.⁵ The existence of laws regulating the mode of transferring wealth intergenerationally does not say anything on how much can be so transferred. This must be determined independently. The paramount requirement to ensure social justice is the primary determinant of the size of the *inheritable* (as opposed to inherited) wealth in an Islamic economy.⁶ In fact, the converse of this statement is even more true: the goal of social justice in an Islamic economy can never be attained without a substantial scaling down to a minimum the size of private property holdings. It may be realized in this connection that in the market-oriented polyarchies of the West, 25 per cent of the national income goes to private property. In fact, most of the inequalities of income can be attributed directly to an unequal

⁵ As Monzer Kahf [3] has pointed out, an important implication of the law of inheritance is that it restricts the ownership of wealth to the life-time of the owners only: the owner has no right even to make a will which contravenes the law.

⁶ It may be noted that the law of inheritance does not by itself exercise a decisive influence on any of the standard coefficients of distribution, e.g. the Gini Coefficient, unless it is assumed that the wealthy tend to procreate more than the poor. In fact, the exact opposite is nearer to the truth. However, as a law, the Islamic law of inheritance is more just than any other such laws found in non-Islamic societies. For instance, a law according to which the eldest son in the family inherits all wealth is clearly inferior in equity to the Islamic law, which allows each member of the family to receive his/her share in a specified proportion.

distribution of wealth [4]. The situation is even worse in most of the developing countries where the prevalence of feudalistic social structures and a low level of literacy exacerbate the evils of a private property system. It follows that since the existence of private property rights is a major barrier to any move towards equalization, private wealth beyond a certain point will have to be collectivized and redistributed. This point is reinforced by the fact that fiscal devices have been singularly unsuccessful in equalizing the distribution of income. The best that can be achieved via this route is to equalize the tax burdens [1].

However, it is important to note in this connection that collectivization of private property is not sufficient by itself to solve the problem of social inequity. It is not too uncommon for State officials to feather their nests at the expense of the society. Thus the need for conscious control is not diminished just because private property passes from private to public hands. It is for this reason that according to Islam the ideal situation is collective control of private wealth by the community (*Ummah*), *as a whole*, and *not* State control.⁷ It, therefore, follows that in an Islamic society, explicit laws must be enacted with a view to: (i) limiting the size of private property to a socially acceptable minimum, consistent with the legitimate human desire to have a modicum of financial security against the unexpected, and (ii) broad-basing the ownership of total wealth. Both these measures will have the effect of activating the institution of private property as a positive element in social dynamics, by keeping in proper balance individual initiative and organizational discipline. Wealth will be more widely distributed and actively utilized for the social good, thus satisfying the requirements of social justice, statically and intertemporally. In this connection, land reforms, which fall short of a complete socialization of all landed property but leave in private hands what can be cultivated by

⁷ It may be recalled that Abū Dharr had vigorously protested against Mu'āwiyā's efforts (651 A.D.) to change the nomenclature of *māl-al-Muslimīn* (wealth of the Muslims) to *māl-Allāh* (wealth of God). Abū Dharr saw in this move a clever plan to appropriate private wealth to fulfil the ruler's ambitions. See Ziaul Haque [2]. The implication of Abū Dharr's position in modern times is that the answer to the problem of private-enterprise capitalism is *not* state capitalism. The Islamic position is to reject both these positions as they are contrary to the Islamic ideal of *al-'Adl*. A sense of participation by the common man in the working of socio-economic institutions through an effective *decentralization of the ownership positions* is an integral part of Islam's economic philosophy. In this sense, the syndicalist's programmes deserve to be studied carefully by the Muslim policy-makers.

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(ii) Ownership of the Means of Production

It is well known in economics that the system of free markets is not sufficient, nor even necessary, to optimize social production or consumption. Market imperfections (e.g. monopolies, external economies, etc.) drive a wedge between market profitability and the social profitability of investment. Hence, State intervention becomes warranted to attain the social optimum. However, this argument does not necessarily imply a complete socialization of the means of production, since it says nothing about the *form* this intervention should take. At a deeper philosophical level, the question of the ownership of the means of production in any society is related to its general attitude towards the institution of private property. Under socialism, the right of private property is denied as all productive resources are owned by the State. State ownership of all resources follows from the denial of private property rights. Similarly, *laissez faire* capitalism, which accepts the individual's right to property as an article of faith, also allows production resources to be owned privately. What is the Islamic attitude in this regard? It should be noted in this connection that the Qur'ānic verse, "Unto Allah (belongeth) whatsoever is in the heavens and whatsoever is in the earth" (2:284), does not necessarily dictate complete State control of all means of production, for according to the Islamic philosophy, man, *in his individual capacity*, is God's trustee on earth. Hence, if ideal moral and social conditions come to prevail, in which every individual fulfils the stringent conditions of trusteeship, man is perfectly capable of holding God's treasures in *trust*.

In general, an Islamic society will use direct and indirect controls to regulate not only the level but also the composition of production and consumption. Exactly in what proportion these two types of

controls will be combined can be decided only at the level of practical policy-making, with an inevitable element of improvisation and *ad hocism*. However, as pointed out several times in this book, it is certain that the State will have to play a very important role in an Islamic economy. An excessive trust in the efficiency of the "invisible" hand (i.e. market forces) is no part of the Islamic perspective; nor is the absolute sovereignty of the consumer the guiding principle of Islamic economics. As pointed out in Chapters 2 and 3, the concept of a free man is quite distinctive in Islam, which reins in freedom by imposing on him the corresponding social responsibility.

(iii) Social Security System

In view of its heavy bias towards social justice, an elaborate social security system must form an integral part of the policy package in an Islamic economy. Every citizen of the country, the unemployed, the old and the sick, must be guaranteed a reasonable level of income *irrespective of his ability to earn it*. The clear Qur'ān commandment, "And in their wealth the beggar and the destitute had due share" (51:19), calls for an effective State machinery to bring about a transfer of resources from the rich to the poor.⁸ This makes eminent economic sense because the system of free markets does not make an explicit provision for institutions which equalize the marginal utility of social consumption. The State must, therefore, intervene to do the job. In particular, once ethical norms are made the dominant requirement in an Islamic society, the responsibilities of the State with respect to utility equalization among individuals should become even more onerous than in non-Islamic economic systems.

However, this process of utility equalization will require a substantial lowering of the top income brackets and a raising of the bottom line, necessitating not only an equalization of income but an equalization of consumption as well. The predominant concern for

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the lot of the poor and the downtrodden is an essential part of the Islamic system: there could be no greater argument for an elaborate social security programme than the fact, noted in earlier chapters, that it is God's Will to favour the weak and the needy. Not only that, *The process of income equalization, buttressed by State legislation, should go on until the poor become honourable members of the society.* A direct implication of this rule is that, at least to begin with, the poor will have to be *unequally* treated.

As for the financing of such an elaborate social security programme, the *Zakāt* tax is already a recognized Islamic policy instrument. It is clearly provided in the Holy Qur'ān that the proceeds of the *Zakāt* levy must be used to alleviate acute poverty by making a direct impact on that section of the society which cannot normally be reached through normal fiscal devices (see Chapter 8). However, if the proceeds of the *Zakāt* tax are not sufficient to finance it, then, according to predominant Islamic opinion, additional taxation should be imposed to achieve the egalitarian objectives of social policy. In the long run, such a policy should pay off in terms of better economic performance as well as a marked improvement in the quality of life in an Islamic economy.

(iv) Growth Policies

As pointed out in Chapter 5, economic growth in the Islamic perspective is a way of ensuring social justice intertemporally and intergenerationally. This is an important point because economic growth can be secured in a variety of ways, all of which are not Islamically-legitimate. In particular, any growth policy which requires an excessively inequitable income distribution must be rejected by the policy-makers in the Islamic economy. A clear instance of such an unacceptable policy is the growth strategy followed by Pakistan, in common with most other developing countries, during the Sixties,⁹ which allowed corporate profits to rise almost without limit. While real wages were not permitted to increase appreciably, no effort was ever made to regulate the excessively large profit margins, which were made even bigger by stringent import restrictions through two routes: firstly, the marginal

⁹ For a detailed discussion of Pakistan's growth strategy during this period, see Naqvi [6].

profitability of the domestic investment of import-substitution industries was raised sharply; secondly, the monopoly power of the domestic producers was substantially enhanced. The combination of these two forces led to the creation of idle productive capacity in the industrial sector. As predicted by economic theory, the monopolistic producers did maximize their profits, curtailing output and raising prices. The common man, on the other hand, suffered because he was forced to buy low-quality and high-priced goods as a matter of patriotic duty. Thus social consumption was not maximized, nor was social production raised to optimal levels. This policy also aggravated considerably the inequalities of income and wealth. An entirely unintended "fall-out" of the policy was that even reinvestment could not be maximized since a lot of these excess funds, which could not be profitably invested, were devoted instead to luxury consumption, financed mostly through imports.

It may be noted in this connection that the policy of encouraging corporate saving amounted to an interest-free loan to the industrialists, who misused it. A low or zero price of capital, much below its opportunity cost, encouraged overcapitalization, excess capacity and allocative inefficiency. From a social point of view, such a policy deepened even more the inequalities of income and wealth; for the profit margins would have been greatly reduced if capital had been priced more realistically. Even worse, a cheap capital policy encouraged the tendency to substitute capital for labour, complicating still further the unemployment problem. Furthermore, due to this policy, the accumulation of excess funds in the hands of the investors made them immune to the State Bank's regulatory policies, which by and large failed to impose on them the socially necessary monetary discipline. During the Fifties and most of the Sixties, Pakistan's economy remained mainly a regime of *laissez faire* in which the State had no useful economic role to play.

It is therefore obvious that an excessive reliance on the corporate sector should be Islamically reprehensible, for the simple reason that none of the stated objectives of an Islamic economy, noted in Chapter 5, can be achieved through this route. It will promote higher unemployment, make State control ineffective, and lead to a gross economic waste and a growing cleavage between the rich and the poor. Clearly, all these results run counter to the Islamic economic philosophy. Economic growth in an Islamic economy can *only* be pursued through a strategy which combines State control of the

means of production with a conscious policy to encourage private initiative. The next chapter deals with these matters in greater detail. Suffice to note here that the State will be a dominant force in an Islamic economy, implying a shift from private to public saving and investment. Furthermore, greater emphasis will be accorded to the human factor in the growth process. From a strictly economic point of view, such an attitude should lead to the selection of "first-best" policies. For instance, in so far as technological change is the crucial element in the dynamics of social change, an Islamic economy must *directly* subsidize the learning process.¹⁰ In general, the emphasis should be on improving the quality of labour which should help the growth process, because higher levels of employment will be generated through lower average capital/labour ratios in capital-scarce economies. In this way, an Islamic economy should avoid the danger of "immiserizing growth" – growth adding to, instead of subtracting from, human misery.

Summary

The broad policy package in an Islamic economy should include more humane policies to promote social justice, statically and dynamically. While the role of individual initiative must be given due recognition, an Islamic economy will generally be dominated by government direction and control of economic activity. The general Islamic approach is to rid existing institutions of their exploitative contents and turn them into active elements in the process of change. While the institution of private property will be formally retained, though on a greatly reduced scale, to satisfy man's innate desire for security, it will not be allowed to become an incubus, fostering *status quoism* and obstructing the process of social change toward a more egalitarian society. The process of growth, rid of its oppressive properties in an Islamic set-up, will maximize social welfare, whereby all social classes benefit *actually*, not only potentially. Furthermore, the human factor should receive the maximum emphasis in the process of economic development. Such a comprehensive social approach, which combines ethical considerations

¹⁰ The common practice in developing countries is to *protect* (through tariff restrictions or direct subsidies) the manufacturing activity to promote technical change. This is clearly a sub-optimal policy. For a full discussion of these matters, see Naqvi [7].

with purely economic ones, will make a maximum contribution to improving the quality of life, both materially and spiritually. It will aim at freeing man from the social degradation that goes with poverty, while inducing him not to forget his responsibility towards the society. In an Islamic society, the economic process, not entirely materialistic, will have to be essentially non-exploitative, with no quarter given to reactionaries who block all social reform for fear that it will be directed against them. A wilful obfuscation of the forces of social change through a reactionary interpretation of the Islamic laws is bound to lead to social upheavals. If Islam is against violence as a solver of social problems, it is even more opposed to forces and policies that make revolutions inevitable.

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means of production with a conscious policy to encourage private initiative. The next chapter deals with these matters in greater detail. Suffice to note here that the State will be a dominant force in an Islamic economy, implying a shift from private to public saving and investment. Furthermore, greater emphasis will be accorded to the human factor in the growth process. From a strictly economic point of view, such an attitude should lead to the selection of "first-best" policies. For instance, in so far as technological change is the crucial element in the dynamics of social change, an Islamic economy must *directly* subsidize the learning process.¹⁰ In general, the emphasis should be on improving the quality of labour which should help the growth process, because higher levels of employment will be generated through lower average capital/labour ratios in capital-scarce economies. In this way, an Islamic economy should avoid the danger of "immiserizing growth" – growth adding to, instead of subtracting from, human misery.

Summary

The broad policy package in an Islamic economy should include more humane policies to promote social justice, statically and dynamically. While the role of individual initiative must be given due recognition, an Islamic economy will generally be dominated by government direction and control of economic activity. The general Islamic approach is to rid existing institutions of their exploitative contents and turn them into active elements in the process of change. While the institution of private property will be formally retained, though on a greatly reduced scale, to satisfy man's innate desire for security, it will not be allowed to become an incubus, fostering *status quoism* and obstructing the process of social change toward a more egalitarian society. The process of growth, rid of its oppressive properties in an Islamic set-up, will maximize social welfare, whereby all social classes benefit *actually*, not only potentially. Furthermore, the human factor should receive the maximum emphasis in the process of economic development. Such a comprehensive social approach, which combines ethical considerations

¹⁰ The common practice in developing countries is to *protect* (through tariff restrictions or direct subsidies) the manufacturing activity to promote technical change. This is clearly a sub-optimal policy. For a full discussion of these matters, see Naqvi [7].

with purely economic ones, will make a maximum contribution to improving the quality of life, both materially and spiritually. It will aim at freeing man from the social degradation that goes with poverty, while inducing him not to forget his responsibility towards the society. In an Islamic society, the economic process, not entirely materialistic, will have to be essentially non-exploitative, with no quarter given to reactionaries who block all social reform for fear that it will be directed against them. A wilful obfuscation of the forces of social change through a reactionary interpretation of the Islamic laws is bound to lead to social upheavals. If Islam is against violence as a solver of social problems, it is even more opposed to forces and policies that make revolutions inevitable.

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Choice of Policy Instruments: Abolition of *Ribā*

In the previous chapter, we attempted to expound the Islamic point of view on certain broad policy issues. We now turn to a detailed consideration of Islamically-legitimate specific economic policies. In this connection, the most important, and yet the most difficult, issue relates to the Islamic position with respect to the abolition of *ribā* (i.e. usury, a positive rate of interest). It is important because the Islamic commandment to abolish it signifies a distinctive socio-economic philosophy, which abhors social exploitation in all forms, including "unbalanced" and iniquitous financial relationships. It is difficult because the abolition of *ribā* is in fact a signal for not only a financial rearrangement but, even more fundamentally, for a restructuring of the entire economic system along Islamic lines.

Nothing less will do. Any Islamic solution that seeks to combine incompatible elements belonging to different economic systems is bound to be counter-productive. For instance, a zero rate of interest cannot be foisted into a capitalistic system. To put it even more bluntly: capitalism cannot be "Islamized" just by abolishing *ribā*. Indeed, it will be unfair to assume that an economic system raised on Protestant ethics will "respond" positively to an injection of Islamic ethical values into it. By the same token, the absence of the institution of interest rate in a socialistic economy does not bring it any nearer to an Islamic economic system, because the reasons for doing so are different in the two systems. In general, the viability of the Islamic position on the use of specific policy instruments, such as *ribā*, is strictly relative to the Islamic economic system.

All the same, Islam is quite clear about what should be done about *ribā*: abolish it: "O ye who believe! Devour not usury, doubling and quadrupling (the sum lent)" (3:130).¹ And there is no option for

¹ Although the translator has used the word "usury" for the original Arabic word *ribā*, it is preferable to translate it as interest. For, according to the near-unanimous Islamic opinion, *ribā* stands for interest, simple or compound. There are some who insist that *ribā* means only usury (or compound interest). However, apart from the epistemological question about what *ribā* exactly means, which the present author is not qualified to answer, the dispute about its real meaning is not really central to the argument in the text.

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believers but to carry out this commandment because "We have prepared for those of them who disbelieve a painful doom" (4:161). There is no doubt, therefore, that *ribā* will not be a part of a *fully-fledged* Islamic economy, which must find an alternative way of handling its economic problems.

Fundamental Considerations

To clarify the basic issues involved, it is essential to keep in view the following points about the Islamic injunction against *ribā*. Firstly, the abolition of the rate of interest is a policy instrument, not a policy objective. This is an obvious but seldom-noticed point. It has two very important implications: (i) the abolition of *ribā* is a means, only one of the means, of realizing in practice the preconditions of an exploitation-free Islamic economy; and (ii) the range of choice of feasible economic policies in an Islamic economy, once a positive interest rate has been abolished, will become restricted to only those policies which do not exacerbate social injustice, in particular those arising out of the inequalities of income and wealth. In other words, the choice of alternative policy instruments must be consistent with Islam's ethical philosophy.

Secondly, while a zero rate of interest may be a necessary condition, it is by no means sufficient to "span" an Islamic economic ordering. In other words, although a fully-fledged Islamic economic system implies a zero rate of interest, the reverse does not necessarily hold. This observation has two clear logical implications: (i) a zero rate of interest occurs whenever an Islamic economic system occurs; however, it is possible that a zero rate of interest occurs even when an Islamic economic system does not occur.² Put together, these two statements suggest that any proposition which asserts that a zero rate of interest is sufficient for the establishment of an Islamic system is false.³ This is because, in a formal sense, socialistic

² In the terse language of mathematical logic: If A (=an Islamic economic system) then B (=a zero rate of interest), does not exclude B occurring without A. Also, B if only A does not preclude B occurring without A. See M.C. Gemignani [2].

³ This conclusion also accords with "commonsense" (based on a knowledge of Islamic economic ethics) because Islam not only prohibits *ribā* but most aleatory (*gharar*) transactions – pure speculative deals, forward trading, etc. Abolishing *ribā* does not automatically lead to the elimination of all aleatory deals – which requires additional action.

societies also have no use for interest as an institution.⁴ Indeed, going a step further, the validity is highly suspect of even the milder statement that the abolition of *ribā*, within the framework of a capitalist economy, will by itself unleash a chain of events leading to its automatic transformation into a fully-fledged Islamic economic system. In fact, it can be validly argued that such an isolated step may lead to a "divergent" movement away from the goal of an Islamic economic system. The basic thing is to bring about a "structural change" in the basic production and consumption relationships, the saving-investment nexus and the process of money creation.

Thirdly, *the abolition of ribā implies, in a deeper sense, a rejection of the entire capitalistic system.* This assertion can be "proved" quite easily. Capitalism is run on the basis of a limited liability to risk.⁵ It should be clear that this principle satisfies the criterion of social justice because the knowledge of the individual about the operations of large-scale enterprises is limited. But limited knowledge must entail only limited risk, which is what a positive rate of interest basically implies.⁶ Hence a positive rate of interest, *in the context of capitalism*, satisfies the criterion of Equilibrium (i.e. social justice in the present context). This is a contradiction because Equilibrium, in

⁴ This way of reasoning is referred to in mathematics as *disproof by counter-example*: We negate a statement by finding an instance, *just one*, where it does not hold. This is a disproof because in order to be true a statement must hold in every circumstance in which it claims to hold. See M.C. Gemignani [2]. It may be noted here that in socialistic societies, a positive rate of interest is used only for accounting purposes – to calculate the relative social profitability of investment projects. However, it does not exist as an institution, in which one set of people lends money to others in the society. In the absence of the institution of private property under socialism, it is impossible for interest to exist in this form. Furthermore, since all saving and investment is done by the State, a positive rate of interest is not required to encourage saving and capital formation. Of late, some socialist countries have allowed interest on personal saving, which remains a minuscule proportion of the total saving. However, this does not vitiate the argument in the text.

⁵ Interest-bearing debentures signify the principle of limited liability, since the holders of debentures are not responsible if a firm goes into liquidation. This is the low-yield option of risk-aversers. Risk-takers go for higher-yielding, but risky, ordinary stocks. Abolishing of all interest-bearing options will, therefore, amount to asking all risk-aversers to become risk-takers. In the context of capitalism, this is not always just.

⁶ As pointed out by Samuelson, "as long as any land or other asset exists with a sure perpetual net income – and as long as people are willing to give only a *finite* amount of money today in exchange for a perpetual flow of income spread over the whole future – we can hardly conceive of the interest rate falling to zero" [13, p. 606]. The reluctance of lenders to lend infinite amounts indicates an unwillingness to take on unlimited liability with respect to the risk inherent in business transactions.

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Fourthly, it should be clearly understood that the focus of Islamic reform is not so much on *abolishing* interest as on *replacing* it by introducing wide-ranging structural changes in the economy along with an Islamically-legitimate financial mechanism. Hence the Islamic injunction against *ribā* does not necessarily negate the Fisherian explanation for the "existence" of a positive rate of interest, viz. the net productivity of the "roundabout" methods of production, and a positive preference for the present consumption over future consumption.⁸ It is only that Islam does not accept it as a *justification* for perpetuating the *institution* of interest – an institution which allows the wealthy to live off interest income. As explained in Chapter 6, it is not the capitalistic "method" of production but the capitalistic mentality that runs counter to Islamic ethics. It follows that the Islamic prohibition of *ribā* is not exactly the Aristotlean or Medieval Schoolmen's concept according to which money is "barren" and hence must not earn any return.⁹ The Islamic

at a philosophical level, every principle, an economic principle for that matter, is both a limited idea and an "unlimited symbol". The universality of any principle, which is essentially a "limited idea", can be established only by reference to what this broad idea stands for, i.e. the "unlimited symbol". In fact, one can go still further: the social utility of any dogma lies in its ability to realize the social objectives implicit in it. This has been pointed out in a different context by Frithjof Schuon [14, p. 7].

⁸ In terms of the Fisherian diagram, measuring present consumption on the horizontal axis and future consumption along the vertical axis, the vertical bias of both the production possibility frontier and the indifference curve explains the existence of a positive rate of interest. If the production possibility frontier and the consumption indifference curve were both made symmetrical around the 45° line, then the rate of interest will be zero. It should be clearly understood that this is *not* necessarily the assumption behind *ribā*'s abolition in Islam. In fact it is shown in the ensuing discussion that the individual's time preference will continue to be positive – i.e. the consumption indifference curves will have a vertical bias in an Islamic economy. However, government action should have the effect of reversing this bias in the individual indifference curves.

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injunction against *ribā* is in fact a special case of a more general rule which prohibits *all* financial deals which promote social inequities.

Finally, it should be clearly understood that a zero rate of interest in the context of an Islamic economy does not denote a state of capital saturation, although this possibility is not excluded from consideration.¹⁰ It will obtain in conditions of capital scarcity as well. This observation should make it absolutely clear that the Islamic commandment to abolish *ribā* in *no way implies that capital will, as a general rule, have a zero "shadow" price in an Islamic economy*. The Islamic injunction against *ribā* is not an arbitrary rule abolishing it through an administrative fiat. It is a much more sophisticated affair. What is involved here is the Islamic rejection of a particular *mode* of capital pricing, namely through a positive interest rate, which offends the Islamic ethical philosophy and must therefore drop out of the set of policy instruments available to the policy-makers in an Islamic economy. It follows that to enforce the Islamic injunction, *alternative means must be found to price capital appropriately*, satisfying the requirements of Islamic ethics.

A Functional Approach

All these considerations lead up to a very important conclusion: it is a *non sequitur* to assert that since, in the Islamic perspective, a positive rate of interest is bad, just any policy replacing it must be good. The "optimality" of any policy alternatives must be established "independently" by reference to the basic policy objectives of an Islamic society. An adequate analytical approach to

Footnote 9 continued

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this difficult problem, which not only highlights the policy alternatives to *ribā* but also establishes their optimality, is to look at the problem from the point of view of the socially desirable functions that a positive rate of interest performs in any dynamic economy. The optimality of a particular policy alternative will then be established by reference to its success in performing these essential functions in the "best" possible way – best in the sense of satisfying the "optimality" conditions, which include the requirements of social justice in an Islamic economy.

It is assumed in the analysis presented below that these essential functions are invariant with respect to the institutional framework postulated – capitalistic, socialistic or Islamic. However, this invariance ceases once we pass on to the question of exactly how these functions should be performed to satisfy the requirements of a growing economy. In a capitalistic economy, a positive rate of interest performs these functions, while socialistic economies have no use for it, except for accounting purposes. In view of its distinctive character, it is interesting to see how an Islamic economy would be doing this job.

It is important to be clear at this point about the distinctive character of the Islamic proposition; Islam prohibits *ribā* but allows *limited* private property rights, both of which symbolize the Islamic moral philosophy of a just society, free of exploitative elements, which at the same time keeps individual initiative intact. However, this complicates the task of the policy-maker in an Islamic economy. His job is definitely much more difficult than that of his counterpart in a socialistic society, which abolishes both *ribā* and private property. It is definitely much more demanding, in terms of human ingenuity and technical skill, than in a capitalistic system, which allows *ribā* as well as the institution of private property.¹¹

Essential Functions

In this analytical set-up, the first step is to "decompose" the

¹¹ These inter-system comparisons should alert the Muslim policy-makers to the fact that, at least in the transition period, the system of private property will have to be greatly de-emphasized since its existence *obstructs* the process of the abolition of *ribā*. This simply illustrates the difficulties of translating the Divine Message onto the plane of social existence. Institutional constraints, which cannot blur the Divine Vision, put definite limits on the manoeuvrability of policy-makers, however well-meaning they may be.

interest rate into a minimal set of economic functions.¹² It can be shown that when a fully dynamic analysis is carried out, the interest rate in a dynamic "real" economy (i.e. the one with no money in it), being equal to the net marginal productivity of capital, must perform three distinct but additive functions: (i) to offset the effects of a positive social rate of time preference on saving and investment; (ii) to compensate for the secular decline in marginal utility of saving owing to its growth; (iii) to provide for the physical depreciation of the country's capital stock;¹³ and, when money is introduced into the system, (iv) to allow for the effects of changing price expectations on the real value of saving and investment.¹⁴

(i) SOCIAL RATE OF TIME PREFERENCE

As is well known, a positive time preference, reflecting the essentially myopic nature of individual's economic calculus, necessitates that the rate of interest be positive. If, on the contrary, the rate of interest is reduced to zero, with a positive time preference, the cost of transferring future income to present consumption will be

¹² Samuelson points out that the market rate of interest has two functions: it rations scarce capital resources in view of the priority of the investment projects, and induces people to indulge in capital formation [13, p. 602]. However, what we wish to do is a more fundamental "decomposition" of the *real* rate of interest, which in fact denotes the marginal rate of substitution between present consumption and future consumption. A detailed mathematical derivation of this proposition is given in Naqvi [9]. The ensuing discussion rests heavily on that paper. The method of derivation is first to decompose marginal net product of capital into what it must provide for, and then to derive the final equation by observing that the rate of interest must, in conditions of dynamic equilibrium, be equal to the current marginal net productivity. The general mathematical approach in the above-noted paper is that of optimal control theory.

¹³ It is important to note that the ensuing analysis is restricted to steady-state (i.e. long-run equilibrium) situations under conditions of certainty. Of course, in real life situations, off-the-steady-state behaviour, under conditions of uncertainty, should be more interesting. However, a full analysis of such situations is beset by the inadequacy of the existing economic knowledge to handle them in a systematic fashion. The only point we have noted below for disequilibrium situations is that *new* investment will also appear as one of the terms in the equation. As for the relevance of such an analysis to an Islamic economy, wherein an element of uncertainty must be allowed for in financial transactions, it may be noted that any "uncertain" situation can be converted into an "as if certain" situation by making an explicit provision for an appropriate risk premium to hedge against uncertainty. Some such rule will have to be devised because "unbounded" uncertainty will make it impossible for any worthwhile economic activity to take place.

¹⁴ This is not to say that the introduction of money into the system is that straightforward. Here, we note only one of the factors that become relevant in a money economy.

this difficult problem, which not only highlights the policy alternatives to *ribā* but also establishes their optimality, is to look at the problem from the point of view of the socially desirable functions that a positive rate of interest performs in any dynamic economy. The optimality of a particular policy alternative will then be established by reference to its success in performing these essential functions in the "best" possible way – best in the sense of satisfying the "optimality" conditions, which include the requirements of social justice in an Islamic economy.

It is assumed in the analysis presented below that these essential functions are invariant with respect to the institutional framework postulated – capitalistic, socialistic or Islamic. However, this invariance ceases once we pass on to the question of exactly how these functions should be performed to satisfy the requirements of a growing economy. In a capitalistic economy, a positive rate of interest performs these functions, while socialistic economies have no use for it, except for accounting purposes. In view of its distinctive character, it is interesting to see how an Islamic economy would be doing this job.

It is important to be clear at this point about the distinctive character of the Islamic proposition; Islam prohibits *ribā* but allows *limited* private property rights, both of which symbolize the Islamic moral philosophy of a just society, free of exploitative elements, which at the same time keeps individual initiative intact. However, this complicates the task of the policy-maker in an Islamic economy. His job is definitely much more difficult than that of his counterpart in a socialistic society, which abolishes both *ribā* and private property. It is definitely much more demanding, in terms of human ingenuity and technical skill, than in a capitalistic system, which allows *ribā* as well as the institution of private property.¹¹

Essential Functions

In this analytical set-up, the first step is to "decompose" the

¹¹ These inter-system comparisons should alert the Muslim policy-makers to the fact that, at least in the transition period, the system of private property will have to be greatly de-emphasized since its existence *obstructs* the process of the abolition of *ribā*. This simply illustrates the difficulties of translating the Divine Message onto the plane of social existence. Institutional constraints, which cannot blur the Divine Vision, put definite limits on the manoeuvrability of policy-makers, however well-meaning they may be.

interest rate into a minimal set of economic functions.¹² It can be shown that when a fully dynamic analysis is carried out, the interest rate in a dynamic "real" economy (i.e. the one with no money in it), being equal to the net marginal productivity of capital, must perform three distinct but additive functions: (i) to offset the effects of a positive social rate of time preference on saving and investment; (ii) to compensate for the secular decline in marginal utility of saving owing to its growth; (iii) to provide for the physical depreciation of the country's capital stock;¹³ and, when money is introduced into the system, (iv) to allow for the effects of changing price expectations on the real value of saving and investment.¹⁴

(i) SOCIAL RATE OF TIME PREFERENCE

As is well known, a positive time preference, reflecting the essentially myopic nature of individual's economic calculus, necessitates that the rate of interest be positive. If, on the contrary, the rate of interest is reduced to zero, with a positive time preference, the cost of transferring future income to present consumption will be

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¹⁴ This is not to say that the introduction of money into the system is that straightforward. Here, we note only one of the factors that become relevant in a money economy.

zero, implying a negative marginal rate of saving.¹⁵ In fact, net dissaving will occur even if the rate of interest is positive but low in relation to a positive and high rate of time preference. The question then arises: is it morally right, and economically meaningful, to keep social time preference positive in an Islamic economy? At the individual level, it should be clear that a positive private time preference can be morally justified since man is myopic by nature. It is God's Will, and a great blessing, that he should remain, by and large, ignorant of future happenings. From a purely economic point of view also, the rate of time preference will remain positive so long as the marginal productivity of capital *now* is positive. This is so because the opportunities for profitable investment, open to the present generation, may not remain available to posterity. A similar argument may not be valid when it comes to the government discounting future consumption. According to the classical Ramsey-Pigou argument, it is not morally right for the government to have a positive time preference because, unlike individuals, it is not myopic [11; 12]. On the other hand, as Marglin has argued, it is undemocratic for governments not to discount the future while individuals do the discounting, since democratic governments must reflect the preferences of the individuals in a given society [7]. This argument does not appear to be decisive because a collective decision, while reflecting individual decisions, need not be identical with them. Even in democratic societies, a collective decision is not simply a "linear combination" of individual decisions, but something more. And that "something more" may have the effect of driving the government's time preference down to zero, or even turning it negative.

In order to reflect an individual's preferences into collective decisions, the government must find a way of averaging them. This exercise will require positing axioms, based on an irreducible value judgement with respect to the ethical biases of a given society. This is because, for purposes of averaging, relative "weights" must be assigned to individual preferences. For, by virtue of Arrow's Paradox of Majority Voting, the democratic procedure does not by

¹⁵ However, if time preference is negative, then saving will be positive even with a zero rate of interest. By the same token, a neutral time preference, with zero rate of interest, will entail a zero marginal rate of saving. However, it should be noted that a few empirical studies by Modigliani, Brumberg and others have shown that the marginal rate of saving may not directly be related to changes in the rate of change in interest rates.

itself supply an infallible rule to force consistency between the choices made by a group with individual choices in that group.¹⁶ However, it can be argued, in favour of the government having a positive time preference, that it will be unethical for governments to impose a zero or negative time preference on society because it amounts to imposing too much of a sacrifice on the present generation for the sake of posterity.

On balance, it can be asserted that while individuals will continue to harbour a positive time preference in an Islamic economy, the government need not do so. There is a strong presumption that its average level will be quite low in an Islamic society also because Islam enjoins "normal" levels of consumption, required to sustain a comfortable living, but denounces in no uncertain terms the squandering of wealth on vain and conspicuous consumption. This will be true both at the individual and at the government level. However, a minimum number of ground rules based on the Islamic ethical axioms will have to be devised with a view to ensuring that consumption patterns remain consistent with the requirements of social justice.

(ii) *PROVISION OF CAPITAL DEPRECIATION AND THE FALL IN THE UTILITY OF SAVING*

The other two functions of a positive rate of interest relate to making an adequate replacement of the capital used up in the process of economic growth, and to the obvious fact that the marginal utility of saving tends to decline as total saving gets bigger through time and the expectation that the investor's future income may be enhanced by a favourable technological change. It should be clear that the Islamic view in this regard should be a positive one, for no economy can grow without these functions being performed in an adequate fashion.

(iii) *CHANGING PRICE EXPECTATIONS*

So far we have discussed the essential functions of a positive rate of interest in a *real* economy. If money is introduced into the system,

¹⁶ Arrow [1] shows that, for example, the transitivity axiom, which is valid for individual preference orderings, may be violated in the case of a group ranking based on majority voting.

then not only relative prices but also the absolute price level will change. Consequently, the present decisions of the savers and the investors will be influenced directly by the price expectations they hold. For instance, inflationary expectations will increase the rate of time preference, which will, in turn, augment present consumption. By the same token, it will decrease net saving in the economy. Furthermore, the marginal disutility of saving will get bigger in absolute value. On all counts, therefore, the rate of interest will be higher in a money economy (in an inflationary situation) than in a real economy. The Islamic view on this point can be fixed by considering the obvious fact that, in periods of substantial inflation, capital values depreciate sharply in real terms. Intergenerational equity demands that means be found to make up for this loss in the saver's purchasing power (see footnote 22 *infra*).

The Islamic Solution

Assuming that the rate of interest will no longer be included in the set of Islamically-legitimate policy instruments, the next question in terms of analytical approach of this chapter is: how best can these essential functions be performed in a dynamic Islamic economy?¹⁷ Here the criterion of the "best" is that the measures taken to replace *ribā* must also be those which make the maximum contribution to the establishment of a fully-fledged Islamic economic system. This is essential, because a zero rate of interest has a definite connotation which is meaningful only within the overall Islamic ethical framework. It has been noted in Chapter 2 that, consistent with the special Islamic meaning of the four ethical axioms – in particular equilibrium and Human Freedom – the State must play a dominant role in promoting the basic objectives of an Islamic economy. The "Islamic solution" given below is based on this value judgement. (The alternative solution through profit-sharing, i.e. *Mudāraba*, is briefly discussed in the Appendix and in the next chapter, reflecting

¹⁷ This manner of asking the question rules out as irrelevant the problem of how to abolish *ribā* through an administrative fiat, without pointing to the Islamically-legitimate alternatives for doing the "job" that interest does under capitalism. Such an arbitrary action, reflecting the mistaken supposition that the shadow price of capital is zero, will be economically disastrous because it will force on the economy a maximum marginal disutility of saving, minimizing investment. This cannot possibly be the objective of a dynamic Islamic economy. For a mathematical derivation of these results, see Naqvi [9].

the author's opinion that this solution, while technically feasible, is not the first-best in the above-noted sense.)

(i) SOCIAL RATE OF TIME PREFERENCE

Let us first see how social time preference can be moved down in an Islamic economy. This problem will have to be tackled both at the moral and at the economic plane. At a moral level, habits of simpler living would discourage consumption. However, this is not enough. The presumption that individuals will *systematically* start preferring future income over present income just by moral restraint is an oversimplification of the problem. As pointed out above, positive time preference derives its plausibility from the hard economic fact that, while present income can be deployed to take advantage of profitable investment opportunities in the future so long as marginal productivity is positive and large, the income accruing in the future cannot be so used to benefit from the opportunities available in the present. To generate positive saving, ways must be found to turn the positive private time preference into *negative* by increasing the cost of diverting future income to present consumption.¹⁸ How can this task of turning a positive time preference into negative be accomplished in an Islamic society? More simply, how to generate positive saving in the face of positive (though much lower) time preference, with the rate of interest at zero? No easy answers can be given. It appears that the solution lies in reducing heavily the reliance on private saving and shifting to public saving in order to perform the essential function noted above with a view to keeping the Islamic economy growing along the steady-state path.¹⁹ The government is not restricted by the "optical illusion" with respect to future possibilities that individuals suffer from. Hence, generating "net" public savings really amounts to converting, through conscious fiscal policies, a positive *private* time preference into a negative *social* time preference.

¹⁸ This is exactly what a positive rate of interest does in a capitalistic economy to generate positive saving: in effect, it turns a positive time preference into negative. Alternatively, one can also think of a positive rate of interest as enhancing the future incomes of savers by making it possible to lend present income for future consumption. In the case noted in the text, a positive rate of interest plays the role of *decreasing* the amounts of future income which can be transferred to present consumption through borrowing.

¹⁹ It follows, incidentally, that any policy which enhances the overall reliance of society on (private) corporate saving must be self-defeating in the context of achieving the social goals of an Islamic economy.

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(ii) MARGINAL DISUTILITY OF SAVING OVER TIME

As savings grow with time, their marginal disutility in terms of the sacrifice of the present consumption tends to decline. A positive rate of interest offsets this psychological erosion of the savings base. When interest is abolished in an Islamic society, this psychological factor will not vanish just like that, *although the rate of decline may be slower* because of a more austere living style enjoined by Islam. Once again, a greater reliance on public saving is the only feasible answer because the government is not so myopic as individuals are.

(iii) DEPRECIATION OF CAPITAL AND NEW INVESTMENT

An explicit provision must be made for the depreciating capital stock to finance a growing economy in a dynamic equilibrium; and for new investment as well when the economy is out of equilibrium. Once again, financing for both will come largely from public savings. Indeed, in order to achieve inter-temporal allocative efficiency, the *government may have to take over completely the management of the capital-goods sector*. This will become necessary because, in the absence of a positive rate of interest, there will be no mechanism left to ration and allocate scarce capital goods among competing uses. The planning agency will have to calculate the shadow prices of capital and use them for making micro and macro investment decisions. However, the consumer goods sector may continue to be in private hands. As a result, a dual price system may come to exist in an Islamic economy: market prices for consumer goods, and shadow or accounting prices for capital goods.²⁰ This sounds complicated; but no easy answers are possible when an existing and tried economic order is being replaced by a new and untried (Islamic) order, to be built up from scratch. However, the suggested alternative is entirely feasible. A failure to evolve some such policy will lead us back to square one, with a positive rate of interest left high and dry! We thus reach the inescapable conclusion that *in an Islamic society the State will have to assume an increasingly greater responsibility to finance the processes of saving and investment*. With lesser

²⁰ On the economic reasonableness of such a dual-price technique, see Oscar Lange [5]. It may be noted that the shadow price of capital can also be approximated by an appropriate tax-cum-subsidy policy or by a system of investment auctioning (see Chapter 8, *infra*). Also imports of capital goods can be rationed just like consumer goods through a system of import duties and quantitative restrictions to reflect scarcity prices.

private saving, the *new* investment will also have to be financed by the government.

(iv) FIGHTING INFLATION

We have noted above that a positive rate of interest performs, though imperfectly, the functions of safeguarding the real value of private saving. Interest income also provides reserve funds to finance the escalation of monetary expenditure on depreciation and new investment. What will be done about these problems when interest is abolished in an Islamic economy? As far as the higher cost of depreciation and new investment is concerned, the State will have to take on the major burden. This does not pose a very difficult problem so long as the tax-base is price-elastic so that tax reserves increase automatically in periods of inflation. The first problem must, however, be tackled in a more systematic fashion. It appears that a system of linking private saving with an appropriate cost-of-living index may provide an answer – perhaps the only answer – to this problem.²¹ True, under certain conditions this may build an inflationary bias into the economy, but the problem has to be faced. Perhaps a system of “imperfect indexing” – which is what a positive real interest rate amounts to – may have to be devised in which the Central Bank partially offsets the decline in the real value of private saving, keeping in view the inflationary situation in the country.²² This will take care of the problem of inflationary bias also.²³

²¹ When it is remembered that, in periods of rapid inflation, interest rates become negative in real terms, the policy proposed in the text should be seen to be productive of better results in terms of its effects on saving generation.

²² The phenomenon of inflation raises the epistemological question about the meaning of the term *ribā*. *Ribā* literally means “an increase”. In the present context, it therefore means an (undue) increase in the original capital through accretions of “service” charges which the debtor agrees to pay along with the original sum. It is important to be clear about whether these accretions, prohibited by Islam, increase the original capital sum in real terms or merely in money terms. When prices are stable, it does not make any difference. However, in periods of substantial price increase, capital values *depreciate sharply in real terms*. While the lender loses, the borrower gains, even making an allowance for interest payments he has to make. No redistributive injustice is involved here. If anything, it is the lender who has reason to complain. If *ribā* also means disallowing an increase in the *real* value of capital, then, as argued in the text, steps must be taken to offset the deterioration in it caused by inflation; and a system of imperfect indexing may be the only answer.

²³ It may be noted that in inflationary periods the real rate of interest tends, in general, to be negative, with adverse effects on saving and investment. The same will happen with a system of imperfect indexing. Hence to *improve* upon the present interest-based system, *perfect indexing* will have to be introduced.

Summary

The abolition of *ribā* is a part of the Islamic policy package to establish a just society – i.e. one which satisfies the four ethical axioms and is rid of the stranglehold of the vested groups whose reactionary attitude promotes social tension.²⁴ However, a zero rate of interest is a property of an Islamic economic system and not of a capitalistic system. Hence, the Islamic commandment to abolish *ribā*, in a deeper sense, is a signal for making corresponding readjustments in all basic economic relations. The essential socially desirable functions of a positive interest rate will still have to be performed in an Islamic economy, presumably with better results in terms of economic growth and social justice. A zero rate of interest is not an option for economic anarchy and stagnation, but is a moral commandment to reverse the economic processes which at present promote gross inequalities in income and wealth, to maximize social good – of course, as Islam sees it.

A possible line of action is to increase substantially the role of the government in the process of saving and capital formation. It must be admitted that this is not the only way of abolishing *ribā*. Other arrangements like profit-sharing (i.e. *Mudāraba*) have also been suggested.²⁵ However, the “superiority” of our approach lies in the fact that the steps taken to abolish *ribā* must of necessity contribute to a structural change in the present-day economic systems along Islamic lines. Such an amphibious approach should also take care of the many contradictions that may arise from a gradual introduction of the elements of the Islamic solution into the non-Islamic economic system, so that the transition to an Islamic economic system occurs in a “systematic” way – i.e. through policies which do not violate the basic ethical values of Islam.

On a general philosophical plane, one plausible criticism of the entire approach of this chapter may be that as economic systems change under the force of the “Islamization process”, the necessary functions which keep them moving may also change. However, this is not really so much a criticism as an admission of the fact that human beings are myopic and tend to project the present (and the

²⁴ Bertrand Russell observed: “The power of lending money gives such great wealth and influence to private capitalists that, unless strictly controlled, it is not compatible with any real freedom for the rest of the population” [12, p. 87].

²⁵ This alternative has been suggested by nearly all the authors on Islamic economics. The best exponent of this point of view is Nejatullah Siddiqi [15].

past) into the future. That being the case, there is no real alternative to envisioning an Islamic economy as an economic system that will perform the very same functions which the present economic systems perform. All meaningful discussion of the future can be conducted only in terms of present knowledge. Granted that an Islamic society may come to perform different functions, nobody can tell what they will be since, to a large extent, this is an empirical question. All we can say as social scientists is that these functions will be performed differently – without *ribā*, that is.

Appendix

Is a Profit-Based Economy Feasible?

Assuming that a positive rate of interest will not be included in the set of Islamically-legitimate policy instruments, the basic question in terms of the functional approach of this chapter is: how should these functions be performed in a dynamic interest-less Islamic economy? One possible answer to this question has already been given in the text. That involves a high degree of regimentation of both the monetary and the real sectors of the economy. The solution is the "first-best" in the sense of also contributing the most to the general process of Islamization. By virtue of pointing to the need for a complete restructuring of the economic process along Islamic lines, this "comprehensive" approach is the most "efficient" in realizing the basic objectives of an Islamic economy. As pointed out several times in this book, the absence of *ribā* is just one element of an exploitation-free economy and has meaning only in this context.

An alternative answer, which is the most widely held – indeed, "universally" accepted – by authors on Islamic economics is commonly referred to as the *Mudāraba* (i.e. profit-sharing) principle. There is no doubt that the principle is Islamically legitimate. According to the dictates of the Islamic ethics – *al-Equilibrium and Responsibility* axioms – financial transactions must satisfy the following two requirements: (i) the two parties to the bargain must get a fair share in total profits in a proportion mutually agreed upon in advance; and (ii) this share should be allowed to vary with the size of total profits – which can be positive, negative or zero. Put together, these principles lead to the general view that rental (not interest) on capital should be a function of profits, which tend to vary with business conditions. Thus the possibility of a certain amount of loss sharing in business transaction cannot be entirely absent from the investor's financial calculus.

Now this view, besides being Islamically legitimate, also makes economic sense. In line with the general approach to Chapter 7, this assertion amounts to saying that profits can perform the function of interest rate in a dynamic economy. Is such a substitution of profit for interest possible? In a formal mathematical sense, the answer is in the affirmative, because in dynamic equilibrium the interest rate

and the marginal profit rate must of necessity be equal.¹ This relationship follows because, in general, the profit rate (or rental on capital) is defined as "pure" interest rate plus a risk factor.² In probability terms, the expected value of the marginal profit rate is equal to the sum of two terms: the expected values of the pure rate of interest which is riskless, and the corresponding value of the risk factor. Now, in an economy wherein the outcome can be predicted with perfect certainty the risk factor becomes zero. Hence, the marginal profit rate must be equal to the pure rate of interest.

However, according to Islamic ethics, an element of uncertainty inheres in all financial transactions. In other words, the risk factor must normally be positive. The crucial question is: how large must this factor be? It should be obvious that the expected average risk cannot be made arbitrarily large; or else, all investment will cease. In particular, all risk-aversers – e.g. those who have only their "nest-egg" savings put away for a rainy day – will be closed off from the investors' market. Now, in so far as the financial health of the economy requires participation of the maximum number of investors in investment activity, mostly small, this is not a desirable state of affairs. For the high risk-takers are only those who have large financial resources. It thus follows that the risk factor must have a least upper bound. How can this condition be satisfied? Simply (although it is by no means simple) by converting an uncertain situation into "as if certainty" through an explicit provision for the risk premium to be sufficiently large to cover the risk.

This consideration is a warning against thinking in terms of a mechanical substitution of profit for interest. It would indeed be dangerous should such a substitution take place *within the framework of capitalism*. For, as pointed out in Chapter 7, capitalism cannot work on the basis of an unlimited liability to risk, which is what the proposed reform will amount to. It follows that if an Islamic economy is ultimately to be run on the basis of a free-enterprise economic system – a view which the present author con-

¹ See E. Malinvaud [7]. The marginal rate of profit is defined in terms of the incremental value of unearned income (minus labour income) which can be decomposed into incremental interest income and the rate of change of pure profits. Since in equilibrium the marginal rate of change of pure profits must be zero, the relationship noted in the text follows logically.

² "Pure" rate of interest is defined as the percentage return which has to be paid on any safe loan or money – it is riskless. A whole spectrum of interest rates for ventures of different riskinesses move up or down as this pure, riskless rate of interest changes.

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Assuming that a positive rate of interest will not be included in the set of Islamically-legitimate policy instruments, the basic question in terms of the functional approach of this chapter is: how should these functions be performed in a dynamic interest-less Islamic economy? One possible answer to this question has already been given in the text. That involves a high degree of regimentation of both the monetary and the real sectors of the economy. The solution is the "first-best" in the sense of also contributing the most to the general process of Islamization. By virtue of pointing to the need for a complete restructuring of the economic process along Islamic lines, this "comprehensive" approach is the most "efficient" in realizing the basic objectives of an Islamic economy. As pointed out several times in this book, the absence of *ribā* is just one element of an exploitation-free economy and has meaning only in this context.

An alternative answer, which is the most widely held – indeed, "universally" accepted – by authors on Islamic economics is commonly referred to as the *Mudāraba* (i.e. profit-sharing) principle. There is no doubt that the principle is Islamically legitimate. According to the dictates of the Islamic ethics – *la Equilibrium and Responsibility* axioms – financial transactions must satisfy the following two requirements: (i) the two parties to the bargain must get a fair share in total profits in a proportion mutually agreed upon in advance; and (ii) this share should be allowed to vary with the size of total profits – which can be positive, negative or zero. Put together, these principles lead to the general view that rental (not rent) on capital should be a function of profits, which tend to vary with business conditions. Thus the possibility of a certain amount of loss sharing in business transaction cannot be entirely absent from the investor's financial calculus.

Now this view, besides being Islamically legitimate, also makes economic sense. In line with the general approach to Chapter 7, this assertion amounts to saying that profits can perform the function of interest rate in a dynamic economy. Is such a substitution of profit for interest possible? In a formal mathematical sense, the answer is in the affirmative, because in dynamic equilibrium the interest rate

and the marginal profit rate must of necessity be equal.¹ This relationship follows because, in general, the profit rate (or rental on capital) is defined as "pure" interest rate plus a risk factor.² In probability terms, the expected value of the marginal profit rate is equal to the sum of two terms: the expected values of the pure rate of interest which is riskless, and the corresponding value of the risk factor. Now, in an economy wherein the outcome can be predicted with perfect certainty the risk factor becomes zero. Hence, the marginal profit rate must be equal to the pure rate of interest.

However, according to Islamic ethics, an element of uncertainty inheres in all financial transactions. In other words, the risk factor must normally be positive. The crucial question is: how large must this factor be? It should be obvious that the expected average risk cannot be made arbitrarily large; or else, all investment will cease. In particular, all risk-aversers – e.g. those who have only their "nest-egg" savings put away for a rainy day – will be closed off from the investors' market. Now, in so far as the financial health of the economy requires participation of the maximum number of investors in investment activity, mostly small, this is not a desirable state of affairs. For the high risk-takers are only those who have large financial resources. It thus follows that the risk factor must have a least upper bound. How can this condition be satisfied? Simply (although it is by no means simple) by converting an uncertain situation into "as if certainty" through an explicit provision for the risk premium to be sufficiently large to cover the risk.

This consideration is a warning against thinking in terms of a mechanical substitution of profit for interest. It would indeed be dangerous should such a substitution take place *within the framework of capitalism*. For, as pointed out in Chapter 7, capitalism cannot work on the basis of an unlimited liability to risk, which is what the proposed reform will amount to. It follows that if an Islamic economy is ultimately to be run on the basis of a free-enterprise economic system – a view which the present author con-

¹ See E. Malinvaud [7]. The marginal rate of profit is defined in terms of the incremental value of unearned income (minus labour income) which can be decomposed into incremental interest income and the rate of change of pure profits. Since in equilibrium the marginal rate of change of pure profits must be zero, the relationship noted in the text follows logically.

² "Pure" rate of interest is defined as the percentage return which has to be paid on any safe loan or money – it is riskless. A whole spectrum of interest rates for ventures of different riskinesses move up or down as this pure, riskless rate of interest changes.

siders to be *contrary* to the spirit of Islamic ethics – then an explicit mechanism must be found to keep down the element of risk within a reasonable limit.

A Proposal

It follows that the basic viability condition of a profit-based free-enterprise Islamic economy is to keep the limited-liability principle intact while introducing the element of uncertainty into financial transactions. One way of satisfying this condition is to have most of the equity financing done by the *nationalized* commercial banks, particularly on behalf of those depositors, especially the “small” ones, who wish to earn more through investment in stocks. These banks will then offer their depositors an investment portfolio, ranging from one hundred percent safe deposits, the *nominal* value of which will be guaranteed by the banks, to more “risky” deposits, which promise varying degrees of returns to the depositors, depending on the element of risk involved. The perfectly safe deposits will *at best* get a zero *real* return, even if these deposits are fully adjusted through a deposit-indexing scheme; but they may also get a negative real return if the cost-of-living adjustment is not one hundred percent. On all other deposits there is a possibility of a positive real return, depending on the degree of risk the investors are willing to take. However, most of the profits attributable to uncertainty will accrue to commercial banks. Only a part of the profits will be passed on to depositors, since their risk will be minimal.

This scheme has the merit that it imposes risk on the investors in proportion to their knowledge of the economic world. The small depositors should court no risk because they know little about the workings of the commodity-producing and financial sectors. By the same token, the commercial banks will take the most risk because of their awareness of the intricate workings of modern industrial ventures. They also know how to minimize their risk by “spreading” it through the selection of an optimal portfolio. Social justice demands some such apportionment of total risk – and total profit income – because there are some investors who are perfect risk-aversers. It makes no sense to force them as well to take risks even on their nest-egg savings. Obviously, they cannot do so and would rather stash away their savings in real estate, gold, jewellery, etc.

In general, the banks and the financial institutions will have to

devise a portfolio containing alternative investment possibilities which are related to a *basic* real profit rate, which shall be zero. This basic rate will normally accrue to the marginal investor, who is a risk-averter. This marginal profit rate will be supported by the government at a level which will be determined by business conditions. All other profit rates on investments carrying varying degrees of risk will change as this basic rate changes. It may be noted that the nationalized banks can *normally* ensure a minimum positive profit on investment because they can easily off-set losses in one line of investment by profits in other lines.

Of course, the problem is much simplified if, as proposed in the text, a large part of the commodity-producing sector is also nationalized – particularly the capital goods-producing sectors. In due course, as managerial and technical skills increase, these industries will be generating positive profits, which will contribute to increasing public saving. The commercial banks will, therefore, be taking risk only on their investment in consumer-goods industries. This system is clearly superior to a wholly equity-based system, which will be highly unstable, adversely affecting the investor's expectations. But more on it in the next chapter.

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CHAPTER 8

Choice of Policy Instruments: Specific Issues

The type of Islamic economy that has been presented so far is remarkably free from the excessive collectivizing zeal of socialism as well as from the individualistic anarchism of capitalism. The Islamic approach, though laying considerable emphasis on the conscious organization of economic and social life, never draws in its web so tightly as to stifle the individual initiative completely. The general outlook is neither vindictive nor permissive, but is definitely regulatory and reformative with ethical fragrance enlivening the environment. True, ethical societies, such as Islam seeks to create, *appear* to be overbearing in terms of their "condescending" outlook on human behaviour, for the individual's unlimited freedom of choice to do what suits him best is no longer accepted as the unalterable law of nature. Indeed, in the Islamic perspective, man does not always know what is best for him: "but it may happen that ye hate a thing which is good for you, and it may happen that ye love a thing which is bad for you" (2:216). Such an attitude, despite its apparent autocratic overtones, promotes an atmosphere of certainty in which the cult of unrestrained, unaltruistic individualism has no place. However, the *creative* instincts of man are allowed to flower so that they can contribute the most to collective welfare.¹ The ultimate thrust of Islamic reform is to press both the organization and the individual, in proportion to the "capacities" of each, into the cause of establishing a society based on the ethical principles of Islam. To achieve such a synchronization of man's many behavioural facets, the State will have to assume a predominant, even a patronizing, role in an Islamic system.

Translated onto the economic plane, the government in an Islamic economy will have to use both "direct" and "indirect" economic

¹ Russell [4] has argued that man's actions are largely controlled by instincts, which are of two kinds: creative and possessive. The success of any organization depends on its ability to control and regularize the latter while providing maximum opportunities for the former through individual or group autonomy.

controls to regulate overall economic activity. Furthermore, in order to ensure a socially desirable *and* Islamically legitimate redirection of productive resources, it will be essential for the government to attain the "commanding heights" of the economy. However, the choice of policy instruments in a fully-fledged Islamic economy will be constrained in two principal ways:

(i) *Ribā*, or anything resembling it, will not be among the set of allowable policy instruments.² As pointed out in the previous chapter, an alternative Islamically acceptable principle of capital pricing will have to be found.

(ii) No policy sustaining, or exacerbating, unlimited private property rights will be allowed.

In general, any set of economic policies which have the effect of permanently creating or exacerbating social inequities, cannot be condoned on any pretext whatsoever – e.g. that of economic growth. For an Islamic economy will be committed not just to the achievement of material prosperity but to enhancing the *quality* of life as well. Subject to these constraints, the policy-makers in an Islamic economy will be free to choose an appropriate policy package, containing direct as well as indirect controls, even though the exact proportion in which these two types are combined must remain a matter of economic expediency.

Direct Controls

In an Islamic economy, the government will have to play a pre-dominant role to: (i) direct investment resources into socially desirable channels; (ii) ensure that the scarcest of real resources – e.g. capital – is allocated most economically among legitimate competing uses; (iii) provide enough, but just enough, monetary resources to accommodate the financial needs of the commodity-producing sector in order to avoid excessive fluctuations in economic activity; and (iv) ensure an adequate provision for those who live below the "poverty line".

² For instance, according to some Muslim jurists, the renting of bare land on a sharecropping basis is also forbidden, because it *resembles ribā*. The selling of a tree with unripened fruits for a fixed sum of money is also prohibited in Islam.

(i) Investment Controls

To make sure that investment activity, in both the public and the private sectors, conforms to the overall socio-economic priorities of an Islamic economy, it will be essential to regulate it in considerable detail. In doing so, it will be essential for the policy-makers to make sure that: (a) capital is priced at its scarcity value to ration it and ensure its most economical use; and (b) private profitability of investment decisions is made to approximate its social profitability to prevent under-expansion of socially desirable production.³ This is particularly true of industries in which sizeable external economies exist. For the satisfactory fulfilment of these objectives it will be necessary to adopt a system which gives discretionary, *but not arbitrary*, powers to the government, while making full allowance for allocative efficiency.

INVESTMENT AUCTIONING

An economically valid procedure for achieving the above-mentioned objectives will be for the government to auction investment authorizations to the prospective investors, through the banking system and financial institutions. These authorizations will be sold to the highest bidders through the market mechanism. Such an arrangement will make it possible for the investors to take into account the scarcity price of capital, which will be high and positive in a capital-scarce economy, in making investment decisions. In order to prevent an unnecessary "cornering" of investment authorizations by a few "resourceful" bidders, and also to reflect social investment priorities, the auctions will take place periodically according to the following scheme.

The government, in consultation with the Planning Agency and other responsible authorities, will parcel out total investment resources into several categories of investment, *to be specified in an investment schedule*. Each broad category of investment in the investment schedule will be assigned an upper monetary limit. Auctioning will stop in a particular category once the monetary limit

³ All the more so, because in an Islamic economy there are restrictions on what can and should be included in the consumption basket. Not all productive activities will therefore be "allowable". It may be noted that, in an Islamic economy, not only the feasibility constraints, but also the "allowability" constraints will be binding. See Chapter 3, *Supra*.

assigned to it has been reached. This system will achieve both of the objectives stated above and ensure that investment resources are not all forced into those uses which are considered to be the most profitable from the point of view of individual investors but have a low social profitability. It will also prevent over-capitalization and excess capacity through an economic use of scarce resources and will make sure that the average capital/labour ratio remains in line with the resource-endowment pattern of the country.

The question may be raised: does this scheme have an element of *ribā* built into it? The answer is in the negative. All that is happening under the proposed scheme is that investors will be allowed possession of investment resources only at a scarcity price. The scarcity price of capital is not fixed in advance: *it is determined by the supply of and demand for investible funds*. The scheme has the added merit that it avoids the arbitrariness that goes with a system designed to control the level and composition of investment entirely through administrative investment sanctioning. Administrative procedures in such a system become tangled for the simple reason that the magnitude of excess demand for capital at the going rate of interest, which is generally low, is too large to be cut down through detailed rationing procedures. The proposed system will perform the rationing function at a relatively low administrative cost since the price of capital so determined will reflect its true opportunity cost.

(ii) Income Distribution Policies

Fiscal, monetary and exchange rate policies affect, directly and indirectly, the accrual of money incomes to various classes of income recipients. This should be obvious enough because all measures regulating income flows must have income distributional implications. However, the problem of income distribution has to be tackled in an explicit way. Corresponding to any specified growth strategy, the entire economic superstructure, involving production, consumption and exchange, must be geared explicitly to the attainment of the most desirable income distribution pattern in an Islamic economy. This must involve such diverse elements as land reforms, a specific programme of maximizing the production of wage goods, and an improvement of the public distribution system, including its extension to the rural poor as well. Such an "amphibious" attack on

the distribution problem, mostly through direct regulatory measures, is essential because not only does growth imply a specific distribution of income, but the reverse relationship also holds: the most desirable pattern of effective demand will produce the socially optimal production mix.

In view of the complexity of this problem, the government will have to: (i) provide basic needs at reasonable prices through the adoption of consumption subsidy schemes which may require the establishment of a network of fair price shops; (ii) initiate wide-ranging land reforms to bring about an equitable distribution of land; (iii) make a co-ordinated effort to improve the living standards of the rural poor; and (iv) provide new job opportunities to the under-employed and landless labourers. Jobs such as the construction of roads, dams, irrigation projects, etc. should help solve the problem of underemployment to a large extent and result in the provision of a basic infrastructure. Another source of employment creation could be small-scale and cottage industries. Incidentally, such a policy will also help lower the average capital/labour ratio, a distinct advantage in a capital-scarce economy.

(iii) Nationalization of Banks

In order to achieve the "commanding heights", the process of monetary creation will have to be controlled directly by the government. In an Islamic economy, the "optimal" money supply can best be determined by the government, since it will also be regulating both the level and composition of production and consumption. Indeed, this follows from the argument of the previous chapter: an active government role in the production process implies an even greater degree of control of the process of money creation. Furthermore, as the objective of the economic policy in an Islamic economy is to provide a framework for growth with reasonable price stability, a nearly complete dovetailing of the financial and the real sectors of the economy will have to be arranged. As pointed out above, such a reform will also be essential for abolishing *ribā* in due course. Added to this is the problem of meeting the "allowability" constraint, which again would call for a credit policy not only to supplement purely economic policies but also to enforce the ethical requirements of an Islamic economy.

(i) Monetary Policy

It may be said that the argument in the previous paragraph does not *necessarily* lead to an unambiguous recommendation for an outright nationalization of banks, since there are indirect ways of controlling money supply and, through it, the level and composition of investment. Unfortunately, an Islamic Central Bank would not have too many "degrees of freedom" in exercising a decisive control on money supply through indirect means for the sheer lack of a sufficient number of policy instruments. The traditional policy instruments, like the Bank Rate and the Open Market Operations, will no longer be permitted in a *ribā*-free Islamic economy.⁴ The only orthodox policy instruments still available to the Central Bank in an Islamic economy will be moral suasion and the power to change the statutory deposit ratios for regulating the lending activities of the commercial banks.⁵

⁴ Open Market Operations, in the strict sense of the term, will not remain meaningful because of the absence of interest-bearing securities in an Islamic economy. All the more so because one of the primary aims of Open Market Operations, namely to influence the interest rate *structure*, will no longer be relevant in such an economy. (It has, however, often been argued that Open Market Operations in the *equity* market should remain meaningful in an Islamic economy.) The argument that these policy instruments are not very effective anyway, even in an interest-based system, is irrelevant since it implies the recommendation that steps be taken to make them more effective. For instance, the Bank Rate in Pakistan remained unchanged (and ineffective) during the 1950's and 1960's; but this observation points to the conclusion that the correct policy should have been to raise it. (It has in fact been raised since then.) What we are arguing in the text is that such a policy instrument, irrespective of its effectiveness in the real world, will not be available to the Muslim policy-makers.

⁵ However, these policy instruments will not provide a really effective handle to the Central Bank for control of the money supply, particularly when excess liquidity exists in the banking system. Furthermore, when, as was the case in Pakistan during the Sixties, banks and insurance companies are owned by industrialists, it becomes well-nigh impossible for the Central Bank to influence, through indirect monetary policy, either the level or the composition of credit creation, which, in turn, greatly impairs its capacity to control the process of money creation. That being the case, the government can hardly exercise any effective control on either the level or the composition of investment in the economy.

PROFIT-SHARING ARRANGEMENTS

It has been noted in the literature on Islamic Economics that, while an Islamic Central Bank will lose the interest rate as a regulatory device, it will gain another policy instrument in the form of profit-sharing arrangements. According to this system, the commercial banks will be participating in productive activities by investing deposit money on an equity-participation basis, sharing in both the losses and the profits. The profits and the losses will then be distributed over the total deposit accounts in a specified proportion.⁶ Firstly, while it is true that the system by itself is Islamically legitimate, this fact does not necessarily mean that it is also the best principle on the basis of which an exploitation-free Islamic economy should be run. The crucial fact that will ultimately determine the feasibility of such an arrangement depends on our vision of the structure of the Islamic economy. For the financial flows merely reflect the physical production and consumption relationships characterising a particular economic system. If these structural physical relationships are Islamically unjust, the superimposition of even an Islamically just financial arrangement may end up making the system even more unjust if only through the chaos that such an artificial symbiosis will promote. This is just a restatement of a point noted several times in this book that capitalism cannot be "Islamized" just by the transposition of a single policy instrument from an Islamic economic system.

The economic viability of the proposed profit-sharing system cannot be established through *a priori* reasoning; it must be tested on an economy-wide basis before any meaningful evaluation of it is

⁶ This is the well-known *Mudāraba* principle, which has been held Islamically valid by Muslim jurists. The advocates of this system consider this to be a complete replacement, as a policy instrument, of a positive rate of interest, an opinion which the present author does not share. A brief discussion of an amended *Mudāraba* scheme is given in the Appendix to Chapter 7. It is interesting to note that, according to Ibn Hazm, the institution of *Mudāraba* is not based on the Holy Qur'an or on any of the Holy Prophet's traditions. It was only a custom of the pre-Islamic Arabs: "*Mudāraba* was practised in pre-Islamic Arabia. The tribe of Quraish had no other livelihood but trade. The old people, women, children and orphans used to give their capital on the basis of *Mudāraba* to the merchants for a certain part of the profit" [2, p. 247]. It is important to note his observation that "all the loss in *Mudāraba* was borne by the capital owner and not by the merchant, who took the capital for the purpose of trade" [2, p. 248].

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possible.⁷ As pointed out in the previous chapter, this is because the return on investment becomes a function of business conditions in general and of the efficiency with which the enterprise is being run. Hence, an element of uncertainty is introduced into the investor's expectations. Hence, to hedge against the probability of a loss, ways and means must be found, through some kind of deposit insurance scheme, to guarantee the safety of the *nominal* values of deposits. If no such explicit risk-insurance system is evolved, not only the banking system, but the entire economy will become highly "unstable", since the proposed system will make it hypersensitive to even small changes in business fortunes. Disturbances originating in one part of the economy will be transmitted fully, indeed in a magnified form, to the rest of the economy, which will, in effect, become a house of cards. Thus the "shock-absorbing" characteristics of the present limited-liability principle, on which the modern banking system rests, will be lost under the proposed profit-sharing system. This will be a big loss, since the policy-makers will, in effect, be losing their capacity for on-the-spot "trouble shooting": economic crises, instead of remaining "localized", will always be "generalized" under the proposed reform.

Secondly, to run the profit-sharing system in an efficient way, it will be necessary to recruit a large technical staff to assess the profitability of investment projects. True, some kind of a scrutiny of the viability of investment projects is done even now, but an economy-wide shifting to an equity-based system will increase this type of job several-fold, quantitatively and qualitatively. Indeed, business firms and banks will have to revise the existing accounting procedures, which at present allow a kind of camouflage operation to be carried out with impunity. The outcome will be a substantial increase in overhead expenses, cutting deeply into the distributable

⁷ It may be noted that the proposed system is being tried on a *limited basis* in some Muslim countries. No authoritative studies are yet available on the operational viability and efficiency of this system. But even if such a system succeeds on a *partial basis*, this is no guarantee that it will do so on an economy-wide basis as well. This is because in the latter case, it will require *all* the savers to become risk-takers, something that does not happen when this system is one of the many possibilities open to investors, the option to invest in interest-bearing deposits being not ruled out. The risk-takers may take this form of investment, while the risk-averse will not opt for it. In this case, the preference structure of the investors remains intact while it does not when the system is adopted on an economy-wide basis. A psychological reform, or rather indoctrination, will be required to make risk-takers of us all. But is it really necessary to go to such lengths? The present author would give a negative answer.

net profit margins. This will result in a lowering of the rate of return accruing to the depositors. Thirdly, even assuming that this system may be used as a replacement for interest-bearing deposits, or even as a mode of lending, it can certainly not be employed as a policy instrument to influence economic activity in the same way as *changes* in the rate of interest are used by monetary authorities. The proposed arrangement does not possess any flexibility in that profit (loss) margins, calculated *ex post*, cannot be varied at the discretion of the Central Bank.

It follows from this discussion that indirect monetary controls will be substantially reduced in importance in an Islamic economy, for the simple reason that not many of the traditional policy instruments will be available, while the ones suggested in their place, like profit-sharing, are not really workable. At least so it appears *a priori*. This leads to the inevitable conclusion that nationalization of the entire banking system is an integral part of the Islamic reform.

(ii) Fiscal Policy

It also follows that, to the extent that indirect monetary controls become less important, fiscal policy will gain in importance for laying out the preconditions of a just Islamic economy. In particular, tax and expenditure policies will become significant policy instruments in the general category of indirect controls. And this may turn out to be one of the strengths of an Islamic economic system, because fiscal policy can in general be more effective than monetary policy in restoring full-employment equilibrium.⁸ Furthermore, as pointed out in the previous chapter, reliance on public saving (investment) will be enhanced at the expense of private saving (investment), implying that a high rate of taxation will be an essential feature of a *ribā*-free, welfare-oriented Islamic economy.

(iii) Tax Policy

In an Islamic economy the primary emphasis will be on broadening the tax base rather than on increasing the tax rates. The Islamic

⁸ It is common knowledge that a tight fiscal policy and an easy monetary policy constitute a superior policy mix to the one in which an easy fiscal policy is combined with a tight monetary policy. The rate of capital formation will tend to be higher in the former case than in the latter case.

ethics demand that, except in a few cases, participation in the activity of giving should be *universal*, i.e. by both the rich and the not-too-poor: "Those who spend (of that which Allah hath given them) in ease and in adversity ..." (3:134). Indeed, there is no way to attain salvation except through giving of what one treasures most: "Ye will not attain unto piety until ye spend of that which ye love" (3:92). Tax rates will have to be raised high enough to equalize the burden on the tax-payers but the marginal tax rates will not be oppressively high: "No-one should be charged beyond his capacity" (2:233). Indeed, once the tax base has been substantially broadened, there will be no need of too high tax rates anyway. An implication of such a reform is that a proper balance will have to be achieved between the so-called direct and indirect taxes. However, the main thing is not so much the balance between direct and indirect taxes *per se*, as the economic consequences of both in terms of the basic policy objectives of an Islamic economy, in particular social justice.

Furthermore, the tax policy will be used *primarily* as a revenue-raising device to allow the government to perform its substantially enlarged role in an Islamic economy. Hence, the income-equalizing and incentive functions of the tax policy will have to be relatively de-emphasized. The incentive function will be deflated in proportion to the decreased importance of private saving and investment. Income equalization will be done primarily by reducing drastically the size of private property and by establishing an elaborate social security system. However, in so far as the private sector does play a role in the production process – mostly in the production of consumer goods – an appropriate *tax-cum-subsidy* policy will have to be evolved to induce a socially desirable and Islamically legitimate composition of production and consumption. (Remember the "allowability" constraint noted in Chapter 3.)

It is interesting to note that such a general approach accords with the modern thinking on public finance which aims at broadening the tax base and lowering the tax rates. Furthermore, the modern taxonomic approach warns against "over-straining" any one policy instrument in the pursuit of multiple policy objectives. Experience has shown that using the tax policy for multifarious, often contradictory, purposes tends to weaken its functions as a revenue-raising device by substantially narrowing the tax base. Furthermore, several studies have shown that a tax policy is particularly ineffective in bringing about an equitable distribution of income and wealth.

The best that can be done in this direction is to equalize the tax burden on the tax payers.⁹ Also, the traditional direct-indirect taxonomy is generally de-emphasized in modern literature on public finance in favour of a more analytical approach relating the total tax package to its effects on equity, capital formation, allocative efficiency, etc.¹⁰

An important element of the Islamic tax policy is the *Zakāt* levy (i.e. poor due), which will be *one of the many taxes* imposed in an Islamic economy. It is levied at a flat rate on all wealth, including income that remains unused for one full year, i.e. savings. Since, except for those who are very poor, all have to pay *Zakāt*, the tax base is greatly broadened, giving the entire population a sense of participation and responsibility. Furthermore, this levy is yet another example of Islam's unitary philosophy in which economic expediencies merge with ethical considerations: the payment of *Zakāt* is also a means of spiritual salvation.

A distinguishing feature of *Zakāt* is that it links tax policy with expenditure policy. Not only its rate and base but also the mode of its expending has been specified in the Holy Qur'ān. Furthermore, since, by and large, *Zakāt* is supposed to be levied and spent at the local level, the link between tax and expenditure becomes *visible*. The tax payers know exactly where and how the tax proceeds can be spent. This should be a great help in improving fiscal accountability and facilitating tax collection, which should be bigger because tax evasion will be minimal.

(iv) Public Expenditure Policy

In the context of a welfare-oriented society, such as Islam's, a conscious expenditure policy assumes great importance, since a tax policy is by and large ineffective in promoting social equity. This is because private consumption, curtailed through compulsory measures and a voluntary renunciation of wasteful expenditure, will have to be replaced by a substantial enlargement of public expenditure. This shift of emphasis, in terms of the resultant change in the composition of total national expenditure, is in accord with the

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requirement that a legitimate and an economically efficient consumption basket be produced to satisfy the needs of the poor.¹¹

The broad priorities of public expenditure should accord with the overall requirement of ensuring social justice, statically and dynamically. A direct implication of this statement is that a judicious division will have to be made between the needs of immediate consumption and the necessity to provide for capital formation. However, constrained by the requirements of financing economic growth, public expenditure, at any given point of time, should aim at equalizing expenditure levels across various income groups. Starting from a situation where gross inequalities of income prevail, the focus of expenditure policy will be on alleviating the lot of the poor, the sick, the old, the unemployed and the orphans. It has already been noted that *Zakāt* proceeds must be spent, as laid down in the Qur'ān, primarily on relieving immediate hardships, without creating a permanent class of hangers-on and social parasites. In fact, there is emphasis in the Qur'ān that the needs of those who are genuinely hard-pressed but otherwise won't ask for help – out of self-respect, that is – must be given priority: “(Alms are) for the poor who are straitened for the cause of Allah, who cannot travel in the land (for trade). The unthinking man accounteth them wealthy because of their restraint. Thou shalt know them by their mark: They do not beg of man with importunity” (2:273).

In general, public expenditure must reflect the “fact” that in an Islamic economy the State must play a substantial role, not only as a catalyst but as an active agent of change, in the dynamic process of moving the economy towards the Islamic ideal. In the area of stabilization policy, the State will also have to engage in large public works programmes to generate employment opportunities in distress areas and also to shore up effective demand in times of depression. Indeed, the appropriate budgetary policies will have to be adopted to lessen excessive fluctuations in the business cycles – *à la* Equilibrium axiom.

¹¹ However, the solution to the problem is not as easy as it sounds. To produce an Islamically-legitimate consumption basket, for which there is an effective demand, cannot be arbitrarily foisted upon the people but must be decided upon through the process of trial and error. Economic considerations, political expediency and ethical requirements will all play a part in determining the “contents” of such a consumption basket – something not fixed for all times to come.

Summary

The policy-makers will have to evolve, through the inevitable process of trial and error and learning-by-doing, an optimal policy package to meet the requirements of social justice in a growing Islamic economy. Direct controls will, in general, receive a heavier weight than indirect controls in the overall policy package. The State will have to attain the “commanding heights” for ensuring that scarce resources are redirected for priority uses, subject to the overall allowability constraint. This will entail nationalization of banks and all or most of the capital-goods-producing industries. Furthermore, direct investment controls will have to be exercised for the same reason. Monetary policy will have to be supplemented by fiscal policy, which will gain in importance as a regulatory device.

It may be objected that a substantial expansion of a socially just and efficient public sector will require a quantum jump in the supply of appropriate expertise. This may be a tall order for most of the skill-poor Muslim countries to meet. True, but the skill gap will have to be explicitly recognized (indeed, created) and gradually closed through the promulgation of universal education, without which the Islamic society will *never* take root. There should be no complacency that all this can be done in a short time. Creating an infrastructure of skills is even more difficult a task to accomplish than putting together socially desirable physical and economic infrastructures. Yet, this has to be done, and let nobody think that it is going to be easy. Restructuring of societies is a hard enough job, *but doing it along ethical lines* is truly a Herculean task. To think that the introduction of *Zakāt* and the abolition of *ribā* will solve all the problems is to put these two significant elements of the Islamic reform out of their essential “general-equilibrium” context of a comprehensive, wide-ranging Islamic reform, which seeks to establish a society or system free of social, economic and moral exploitation.

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The Islamization Process

PART IV

OPPORTUNITY AND TEMPTATION

“That ye shall journey on from plane to plane”
The Holy Qur’ān (84:19).

The Islamization Process

It is now time to formulate a definite point of view on the character and message of the Islamic Economic Reform. It may be pointed out that this point of view is not necessarily unique, in the sense of being the only one possible.¹ Other scholars may have a different opinion on the various issues raised in this essay. However, it is hoped that, within the analytical framework laid out in this book, the many deductions with respect to the basic principles of Islamic economics are logically valid and Islamically legitimate. The latter property of these deductions is guaranteed in advance because the fundamental axioms from which they are derived have been shown to be the necessary and sufficient conditions for an Islamic economy.

The preceding six chapters first established a strong plausibility of the existence of an Islamic economic system, which is not necessarily antagonistic to the existing economic systems. From that vantage point, they have outlined broadly the fundamental characteristics and features of an Islamic economy.

¹ Khurshid Ahmad has forcefully argued that we must be prepared to admit "the possibility of a multiplicity of approaches/models, *although with a central core of unity and uniformity*" [1, p. 226]. The italicized phrase is important since it is meant to highlight a basic point regarding the character of explorations into Islamic economics. While the researchers are free to adopt whatever route they wish to take for realizing the basic objectives of an Islamic economy, the freedom is not unlimited with respect to either the choice of policy instruments or the basic policy objective of an Islamic economy. As pointed out in earlier chapters, both the means and the ends must be Islamically legitimate. For instance, there is an absolute prohibition of *ribā* as a policy instrument; it, therefore, drops out of the policy package in a fully-fledged Islamic economy without any further question. Also, the ultimate objective of an Islamic economy is to establish a society based on *al-'Adl* (i.e. Equilibrium). Once again, any policy that defeats this objective can find no place in the thinking of a Muslim economist. However, exactly what strategy should be followed to achieve an interest-free, just society dedicated to *al-'Adl* admits of "multiplicity of approaches" implemented in carefully graduated steps. Despite these restrictions, the intellectual "grazing ground" for the Muslim economists is immense. It has taken the present author a whole book merely to highlight the nature of the problem and its complexity. To do full justice to this stupendous undertaking will require the joint and sustained efforts of the best Muslim minds.

The "Transition" Period

A long distance – spatial, temporal, and intellectual – separates us from the Islamic El Dorado. Inevitably, a "transition period" must intervene before the Islamic economy can be made fully operational.² It would involve unceasing intellectual effort to recognize the "best" way of reaching that ideal through a conglomeration of social and economic forces which achieves material prosperity and spiritual bliss within the unitary framework of Islamic thought. In many ways, the transition period is the most interesting and the most challenging part of the total effort required for a complete Islamization of the present-day societies. This period will be difficult and long, although, depending on the will of the people, its length may be contracted or protracted. The attainment of the all-comprehending Islamic ideal cannot be a one-shot affair. Islamization is essentially a process which unfolds its blessings only gradually.³ This is because to move towards the goal of a fully-fledged Islamic economic system, ways and means must be found to break loose from the "gravitational pull" of the existing economic systems and, even more fundamentally, of the traditional mores and conventional modes of thought. At the philosophical level, the problems of the transition period arise from the difficulty of accommodating an unfettered and immaculate Divine Message into the straitjacket of time-bound and man-made institutions. True, Divine Will demands perfection, which leaves no room for any inconsistencies, yet, at the level of human existence, this perfection remains an ideal to be approximated in stages with varying degrees of success and imperfections that characterise all human solutions. It is clear, therefore, that any attempts at Islamization which involve a precipitous break from the past, however inglorious and morally reprehensible, are bound to lead to gross social and intellectual confusion.

It is important to recognize that such a gradual approach may

² Khurshid Ahmad [1] highlights the transition problem by distinguishing between an Islamic economy and an *Islamizing* economy, the difference between the two being an indicator of the transition period. See also Naqvi [6].

³ Here an "evolutionary" approach to Islamization is implied. If the Islamic system is implemented within the context of a complete social revolution, as it has recently been in Iran, then the Islamization process may be considerably shortened.

introduce "internal" contradictions of its own because, during the transition period, policy instruments which properly belong to an Islamic economic system may have to be grafted on to the existing economic systems. For instance, it is easy to conceive of situations in which such a grafting operation may actually worsen social welfare by enhancing economic inequities. Hence, Islamic reform, instead of moving society towards the ideal State, may push it away from the final goal. And this may happen *even if the policy instruments are Islamically legitimate*. It is, therefore, essential that with a view to minimizing such contradictions, Muslim policy-makers evolve, for the transition period, a viable sequential economic strategy in conformity with the broad Islamic ethical axioms. This must be done on the clear understanding that a "second-best" policy package – i.e. *the one which does not necessarily contain all the elements of the "first-best" alternative* – may have to be adopted to ride out this period.⁴

The Policy Package

The "Initial" Conditions

How best to minimize such "contradictions"? The answer lies in concentrating first on enhancing the quality of social justice, both absolute and relative, by changing gradually the *structure* of the existing societies in Muslim countries to bring them into conformity

⁴ It may be interesting to note in this connection that even the Holy Prophet (Blessings of Allah and peace be upon him) took a cautious approach with respect to the social problems of his day. For instance, slavery was tolerated, even though its existence violated one of the basic messages of Islam – equality of mankind in the eyes of God. He did not abolish it straightaway, perhaps because in those days the "services sector", apart from farming, must have accounted for a predominant share of the total GNP. However, all efforts were made to gradually erode this system by providing that the freeing of a slave was the hallmark of a pious Muslim. Furthermore, steps were also taken to "humanize" the system by ordaining that the slaves must be treated as ordinary human beings. In fact, even in his own household he set an appropriate example for other Muslims to follow: while providing a slave maidservant to his saintly daughter, Fatima, the Holy Prophet (Blessings of Allah and peace be upon him) exhorted that the housework should be done on alternate days by Fatima herself. Even this "limited" step was revolutionary in those days, and remains so to this day in a large part of the world where men are discriminated against on the basis of race or the colour of their skin.

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with Islam's ethical values.⁵ Such a step will be in conformity with the Divine Commandment: "And We desired to show favour unto those who were oppressed in the earth, and to make them examples and to make them the inheritors, and to establish them in the earth..." (28:5-6). In general, the task of the present Muslim generation will be to put together the best possible programme for laying out the most appropriate "initial conditions" (in terms of equalizing the economic conditions within, and among, various classes of the society) for a fully-fledged Islamic economy. Like mathematical dynamical systems, the direction and character of social progress towards the Islamic ideal will be uniquely determined by the choice of "initial conditions".⁶

The importance of creating a just social order by an explicit recognition and enforcement of the best possible initial conditions can be appreciated by the fact that no sensible social reform can become really effective without implementing them. Take the case of education. It is well known that education is an income-equalizing factor of considerable force. However, this requires that the initial endowments of wealth also be equal. If not, *education may itself become a de-equalizing factor*, since the children of rich parents will get better education and, therefore, higher income than those of poor parents. Indeed, the pleas for "equalization of opportunities" made by so many social philosophers will remain hollow without a substantial reduction in the absolute level of income inequality.⁷ The capacity to make effective use of opportunities, even when they are presented equally to all, depends on the degree of effective social participation by the members of a society, which in turn is determined

⁵ Inter-class and intra-class equalization of the economic conditions is essential not only to restore social justice but also to guarantee human freedom. This has been observed by many an acute social philosopher. For instance, Alex de Tocqueville [11] had pointedly remarked that liberty was inconsistent with gross inequalities of "social conditions". Furthermore, Lindahl [4] emphasized the importance of the "just distribution of property to begin with", to lay the preconditions of securing equity. The most influential recent contribution emphasizing the importance of an "initial just order" is, however, that by John Rawls [7].

⁶ In dynamical mathematical systems, once a set of starting values leading to acceptable terminal values has been specified, it is possible to determine an entire time path of the variables that satisfy the necessary conditions for optimality. The dynamics of social systems is broadly similar in character, even though the outcome of specific policies cannot be as infallibly predicted as in mathematics.

⁷ For a detailed demonstration of this thesis, see Jencks [3]. Another influential voice in this vein is that of Thurrow [12].

by their levels of income, past and present. This point must be very carefully noted by those Muslim economists and social philosophers who emphasize that the policy objective in an Islamic economy is an equalization of opportunities, not of income. *If not properly qualified, such an attitude is inconsistent with Islam's ethical philosophy.* Indeed, it is hypocritical, reflecting as it does a thinly disguised championing of the cause of the privileged in the society.

Hence, a policy package relating to the "initial conditions" must focus on: (i) equalizing the distribution of wealth, mainly a sharp reduction in the size of private property, particularly landed property; (ii) reorganizing industrial organization to minimize exploitative elements by making labour's share a function of the total profits of the industry; (iii) making an explicit provision for institutions, in particular an elaborate social security programme, to help those living below the "poverty line"; and (iv) taking decisive steps towards universal education. An effective and honest implementation of these policies should set out the preconditions of a socially just and dynamic Islamic society. These matters have been discussed in previous chapters. However, a few elucidatory remarks on their relative importance during the transition period should help clarify the basic theme of this chapter.

(i) PRIVATE PROPERTY

From the arguments of Chapter 6, it should be quite clear that a substantial dilution, through direct and indirect policies, of the institution of private property must form the kingpin of any egalitarian Islamization programme. This is particularly true of those Muslim countries that live under oppressive feudalistic systems. The most objectionable element of the private property system is landed property, which serves no useful economic functions whatsoever. No economic harm will be done – indeed, great social benefits will flow – if all landed property were to be confiscated by the State in one clean sweep and cultivated on its behalf. Such a step will be strictly in conformity with the Islamic ethical axioms. From a social angle, a case can perhaps be made out for limited private land holdings by owner-cultivators; but the ownership of large land holdings by those who do not cultivate them themselves but live off their rents is both immoral and economically inefficient. Indeed, according to some Muslim jurists, renting out of bare land

for a fixed sum of money is prohibited in Islam because of its resemblance to *ribā*.⁸

The recommendation for a confiscation of big land holdings gets support from the circumstantial evidence to the effect that most of such property was obtained in the past as a reward for the anti-social services rendered by their recipients to the governments of the day. The mere fact that this immorally acquired property was bequeathed to posterity in an Islamically legitimate fashion could not confer any sanctity on such private land holdings. It also follows that the present-day practice of the State in granting fertile land as a reward for rendering the so-called meritorious service must also be discontinued, particularly because the scarce fertile land thereby gets allocated to those who are the least fit to make effective use of it.⁹

In case an *immediate* across-the-board confiscation of all landed property by the State is not considered politically feasible, careful thought must also be given to a policy of gradually weakening the base of the private property system through severe fiscal redistributive measures. In particular, the imposition of capital-gains taxation on landed property should be fully justified – all the more so in a period of rapid inflation and steady urbanization since both tend to escalate the capital values of real estate. The tax money could then be used for the financing of an ambitious social security programme, which forms an integral part of an Islamic economic system. Such fiscal measures will be a positive gain to the society since resources will be transferred from those for whom the marginal utility of income is relatively very low to the beneficiaries of the social security system for whom it is very high.

(ii) VOLUNTARY COMBINATIONS

It is important that some co-operative arrangements be gradually

⁸ Indeed, the eminent Muslim jurist Ibn Hazm (d. 456 A.H.) stoutly opposed the practice of fixed rents. Instead, he favoured a system of pooling the total produce of land and distributing it among all the participants in the production process in a pre-assigned and voluntarily agreed-on proportion. We propose in the next section a similar system for the industrial sector, which, at an advanced stage of economic development, includes agriculture as well.

⁹ Indeed, in the early Islamic period, the free gift of land was limited only to "dead" lands, which could then be reclaimed by the owners at their cost. It was only during the Umayyad period that doling out of top-quality lands was started, mostly to members of the royal family, as a system of concealed bribery. Such practices can never be justified on moral, economic or social grounds.

introduced in the commodity-producing sectors to minimize the reliance of the Islamic society on the competitive system, which, while ensuring a modicum of allocative efficiency, works against both equity and social justice.¹⁰ This is because free competition rewards those who succeed much too liberally, while it penalizes the losers in the game very heavily. An Islamic society will definitely strive to steer clear of such extremes by reducing both the reward for success and the penalty for failure. Such an attitude is strongly indicated because success or failure is not entirely attributable to merit or to the lack of it on the part of the "economic agents". Chance factors and pure luck intervene most of the time to decide the outcome of the relentless struggle for economic survival. Hence, as a part of the Islamization programme, it will be highly desirable, indeed essential, to reorganize the industrial sector along some kind of a two-tier system, which will allow the wage earner a portion of total profits as a bonus in addition to his fixed wage. This system can work effectively to increase the productivity of industries in the public sector. It should promote a sense of effective participation by those who really work by minimizing the "alienation" phenomenon noted by Marx and by promoting social harmony and a sense of responsibility. Such a participatory system should in due course evolve into one in which *all* profits are distributed to the shareholders, minus the financial provision for capital depreciation and a fixed contribution to the national exchequer. These arrangements should make an important contribution to democratize the industrialization process, with powerful built-in incentives for those who make an extraordinary contribution to production. Furthermore, in due course, such arrangements will contribute to changing *power relations* in the industrial sector, a process that should supplement the government's efforts to transfer the ownership of the means of production and property to the public sector with a view to bringing about an egalitarian Islamic society.

¹⁰ As is well known, free competition helps society only to attain a point on the "efficiency locus", thereby satisfying a marginal welfare condition. However, each point on the efficiency locus is consistent with a different distribution of income, which may diverge sharply from the social optimum. Hence, it is necessary to specify a "first-best" distribution of income to attain "social bliss" – a state which will be differently defined in each society *in keeping with its ethical norms*. Furthermore, the maximum welfare thus achieved will not be unique, without specifying the distribution of income, which is determined not by marginal conditions but by the ethical norms of the society. See Naqvi [6].

(iii) UNIVERSAL EDUCATION

A decisive move towards universal education must form an essential component of the "initial conditions" for enhancing the quality of the growth process. As discussed in Chapter 5, Islam lays the maximum emphasis on improving the faculty of thinking in God's universe.¹¹ Inequality among men, in the Islamic perspective, can be justified, if at all, only on the basis of the differences of knowledge among men. However, all modern studies on the economics of education point out that education by itself does not reduce inequality, which is mostly due to income from inherited private property. Indeed, as noted above, the equalization of opportunities of education can be socially beneficial *only* within the framework of an overall Islamic reform aiming at equalizing the economic conditions of the people. It will therefore be essential, at least to begin with, to provide for *unequal* opportunities by committing larger financial resources and physical facilities for the education of the poorer children. Nothing substantial in terms of either material growth or spiritual advancement can be achieved on the basis of the educational standards prevalent in most of the Muslim countries. Hence a sharp increase in financial allocation for education will be required along with a definite programme aiming at the maximum equalization of income and wealth.¹²

(iv) THE ABOLITION OF RIBĀ

The abolition of *ribā* has often been mentioned by Muslim scholars as a part of the policy package aiming at establishing the most appropriate "initial conditions". However, as pointed out in Chapter 7, the abolition of *ribā* can be meaningfully carried out *only* in the context of a comprehensive restructuring of the present-day economies. That will involve nationalization of the entire process of monetary creation and the capital-goods sector and a substantial rise

¹¹ It may be noted that after the word "Allah", "knowledge" is the second most-repeated word in the Holy Qur'ān.

¹² It is interesting to recall in this connection the historic U.S. Supreme Court ruling which maintained that school segregation led to unequal performance even when the schools were of equal standards. Hunt's seminal contribution [2] confirmed the thesis that educability is directly related to socio-economic status and intelligence. T.W. Schultz's pioneering work [10], which analyses the economic effects of education, points in the same direction.

in the proportion of public saving in total saving. Along with the social reforms indicated in the previous section, these steps should transform the entire societal structure along Islamic lines. The institution of *ribā* will then gradually fade away because of its sheer irrelevance in an Islamic economy. However, it is important to bear in mind that *the abolition of ribā is not powerful enough by itself to engineer a smooth transition from an interest-laden economic system to an exploitation-free Islamic economy.*¹³

There is a strong presumption that if such a step is taken precipitately within a capitalistic framework, it may increase, instead of decreasing, the exploitative tendencies in the society, even though the policies replacing *ribā* may be Islamically legitimate. This is because the legitimacy of any policy alternative to *ribā* does not by itself establish its "optimality" in the Islamic sense—i.e. by satisfying the ethical axioms in addition to the purely economic requirement of efficiency. Take the example of a hire-purchase system. In the opinion of some Muslim jurists, this arrangement is a valid replacement of *ribā* because it is different from money transactions which, according to them, must be strictly on a one-to-one basis. It should not take too much ingenuity to understand that the economic burden on the buyer can be made much higher than in an interest-based system by manipulating the terms of hire-purchasing, which also clearly imply *ribā*.

Another example of a "suboptimal" replacement of *ribā* is the oft-suggested system of profit-sharing (see Appendix to Chapter 7). Such a system may lead to various malpractices. The capital suppliers, who may be men of ordinary means, may be defrauded of their "nest-egg" savings by borrowers, who may be rich men, through intricate accounting procedures. At any rate, no sanctity attaches to "profits", which may assume different meanings depending on the organizational structure postulated.¹⁴ In the context of capitalism, wherein labour works for a fixed wage, profits can be

¹³ This follows from the observation made in Chapter 5 that the abolition of *ribā* is a necessary but not a sufficient condition for an Islamic economy. In other words, any statement that the "abolition of *ribā* will of necessity lead to an Islamic economic system" is false. It cannot be emphasized enough that this statement is true only in the transition period. Once a fully-fledged Islamic economic system is established, *ribā* will find no place in it.

¹⁴ The existence of positive profits, in a regime of perfect competition, is possible (i) if uncertainty about the future outcome of economic actions prevails, and (ii) due to the "incidence" of innovations. See E. Malinvaud [5, Chapter 11]. However, in both cases, the excess profits are attributable to entrepreneurship rather than to capital.

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even more exploitative than interest. In fact, the term profit as it is understood today is the product of Sixteenth century capitalism when employment for wages became the cornerstone of a civilization marked by a division of people between capitalists and wage-earners. It is interesting to note that Karl Marx had singled out profits as the worst feature of the capitalistic system, symbolizing exploitation of the poor by the rich, and contributing to the "alienation" of man (i.e. the wage earner) from his environment.¹⁵ By contrast, the term has an entirely different meaning in the case of voluntary combinations, where labour does not work for a fixed wage but receives a specified share in total profits.¹⁶ It follows that an uncritical opting out of the interest-based system for a profit-based system, *without specifying its institutional context*, would be a dangerous proposition on which to raise the superstructure of Islamic economics.

Summary

Much of a society's success in ushering in a fully-fledged Islamic economic system will depend crucially on the character of the steps taken to *initiate* the Islamization process. If we get stuck with less fundamental or relatively trivial matters, leaving untouched the vested groups in the society, then the entire process of Islamization will be gravely endangered, if only for want of its popular appeal. What we should be aiming at instead is to lay the *foundations on which the edifice of an exploitation-free Islamic economic system can ultimately be raised*.

Nothing short of a decisive restructuring of the production and consumption relations will have to be attempted to achieve a decisive breakthrough in the "right" direction. Steps taken to strengthen the effective demand of the poor must be coupled with explicit measures for reorientating the production structure to produce, *within the allowability constraint*, the socially desirable consumption basket. The means of production will have to be largely nationalized and the

¹⁵ True, Karl Marx overplayed the exploitative character of profits, but, as Joan Robinson [8] noted, the neo-classical economists have not been able to completely supplant the basic Marxian thesis. Nor have they been able to produce a more satisfactory theory.

¹⁶ An Islamic society, aiming at combining individual initiative and government control — through its distinctive conception of human freedom — will promote such voluntary combinations. Many an acute social philosopher has noted this. Bertrand Russell, for one, felt that "all institutions, if they are not to hamper individual growth, must be based as far as possible on voluntary combinations..." [9, p. 25].

process of monetary creation consciously regulated to meet the needs of an Islamic society. In particular, not much can be achieved by way of Islamization, unless the present capitalistic structure, along with its capitalistic mentality, undergoes a profound transformation.

The primary emphasis of a meaningful Islamization programme will have to be on reducing the absolute and relative levels of social and economic inequities, without which no other social reform — e.g. a greater provision for education, an equalization of economic opportunities, etc. — can ever produce the desired results. To emphasize isolated policies instead of a wide-ranging structural reform, is bound to be self-defeating. In particular, any programme of Islamic Reform which does not include among the "initial conditions" a satisfactory and just solution of the problem of private property is bound to fail in the long run through sheer lack of public support and enthusiasm. Of course, nothing can legitimately be done in the name of Islam just to elicit popularity by compromising its basic principles. It is just a question of initiating the Islamization process in a way which is Islamically legitimate and has the added merit of mobilizing popular opinion in favour of such a programme, focusing on the amelioration of man's life in relation to his environment.

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The Summing Up

With the help of the analytical tools of Islamic ethics, a modest attempt has been made in this book to spell out the central characteristics of an Islamic economic system. We have used the axiomatic approach as the basic organizing principle. From a “spanning” set of ethical axioms – which are not derived logically from other principles but from which everything else can be deduced – a set of Islamic principles of economic behaviour has been shown following logically. The chief merit of this axiological approach is that it highlights the basic linkage between ethics and economics. It also helps to establish the Islamic (or un-Islamic) character of any economic position by reference to the fundamental ethical axioms. From an analytical point of view, this is a decisive advantage because it would be both impractical and counter-productive to reach out, each time we wish to say anything useful or new on Islamic economics, for the “expert” opinion of those casuists and Muslim scholars who lived in a bygone age. While some such “referencing back” may sometimes be inevitable, it is not always very helpful in grappling with the vastly complicated problems of today. The task of the modern Muslim economists is much more difficult: *at the most fundamental level, the four basic precepts of Islamic ethics must be “rediscovered” in terms of the best that modern thought has to offer.* In the process of this rediscovery, modern civilization will itself undergo a profound transformation on contact with the basic verities of Islam.¹ The laws of social dynamics do not tolerate sharp discontinuities, but flow serenely and continuously from the darkness of the distant past into eternity. This is *not* to say that the immutable ethical principles of Islam must be bent or compromised to suit the dictates of the modern age. The basic

¹ This is the basic message of the so-called “generalized Heisenberg Principle”, according to which the essential inputs and outputs of information cannot be changed with respect to an unchanging system. See Kenneth Boulding [1, pp. 120–121].

Islamic orthodoxy, rooted firmly in the Holy Qur'ān and the tradition of the Holy Prophet (Blessings of Allah and peace be upon him), cannot be tampered with. Yet, all the non-Prophetic interpretations of the Islamic message can be questioned in terms of their relevance to the vastly intricate problems of today and tomorrow.² It is this *right* of an individual to question and even discard traditional wisdom which has ensured the intellectual vitality and dynamism of the Islamic message through the vicissitudes of history during the last fourteen hundred years.

In this brief essay we could not hope to draw a complete and absolutely clear picture of a fully-fledged Islamic economic system. At any rate, our objective has been only to take the first decisive step in the direction of thinking out afresh the basic Islamic philosophy of man's economic behaviour and providing answers to a few difficult problems, without any pretensions about these answers being the only ones possible. It is hoped that in these pages a foundation has been laid for other more knowledgeable Muslim scholars to build on. In the process of idea formation there is no such thing as the final word or a definitive answer. As Frank Ramsey, the philosopher-mathematician, once pointed out, we could never hope to make anything absolutely clear; however we can make a lot of things clearer. This has been our aim, since man can achieve no more. We have aimed at introducing a scientific method of analysis, which explicitly recognizes *normative* principles as valid bases of logical deduction about Islamic economics. The crucial point of our analysis has been that, instead of an *ad hoc* approach, an "objective" principle of selection that also satisfies the binding ethical constraints of an Islamic economy should be made the basis of valid economic propositions. A fuller development of this new subject will require an active two-way interaction between abstract theorizing and empirical verifications of the basic hypotheses.

The axiomatic approach, using the deductive method to derive the basic economic propositions relevant to an Islamic economy, has been employed in this book for three reasons:

(i) Embryonic Islamic economics, which originated with Fārābī,

² Iqbal's observation in this regard is worth noting: "The only course open to us is to approach modern knowledge with a respectful but independent attitude and to appreciate the teachings of Islam in the light of that knowledge, even though we may be led to differ from those who have gone before us" [3, p. 97].

Tūsi and Ibn Khaldūn,³ was deprived of the benefit of evolutionary growth even in the Middle Ages, and could not, therefore, blossom forth into a fully-fledged Islamic economics.

(ii) All subsequent developments in economics took place in the West. Problems arise for the Muslim economists because, while the existing store of Western economic wisdom should not be ignored, all of its principles cannot be assimilated indiscriminately into the Islamic fold.

(iii) Islam has its own distinct, unified view of life based on its all-comprehending ethical principles.

However, these principles must be "condensed" into a consistent, simple and "adequate" set of axioms to derive from them the Islamic view of economic behaviour. It has been shown that the elements of this set are Unity, Equilibrium, Free Will and Responsibility. A logical link exists between them and the basic rules of economic behaviour in an Islamic economy. With the help of this analytical method, it has been shown in this book that an Islamic economic system "exists", as distinct from all existing economic systems, like socialism, capitalism and the welfare state. However, it is one thing to say that Islam offers a distinctive economic system, but quite another to assert that it is self-sufficient in the sense of being isolationist. In fact, Islam clearly rejects such a Spenglerian view of social dynamics, according to which social systems develop in complete isolation from each other and with little interaction among them.⁴ The Islamic attitude is not one of valetudinarian narcissism in the realm of ideas but is based on a healthy exotericism, which is ever watchful of intellectual advancement and only too eager to assimilate it, *so long as its distinctive esoteric ethical foundations are not compromised*. Islam, being the last revealed religion, has the special power of synthesizing past and present wisdom, transmuting it into its own mould through a definite process of "selection" and then improving upon it before finally accepting it: evolutionary syn-

³ It may be interesting to point out, as an historical anecdote, that Ibn Khaldūn anticipated 400 years ago the essentials of Adam Smith's message on the superior benefits of division of labour in increasing the productivity of economic organizations [2].

⁴ The falsity of the Spenglerian argument can also be established by an historical study of the evolution of social systems. Toynbee, commenting on the general course of English history, in his *magnum opus* concludes that "the farther back we look the less evidence do we find of self-sufficiency or isolation" [5, p. 2]. He approvingly quotes Lord Acton: "General history naturally depends on the action of forces which are not national but proceed from wider causes."

thesis lies at the heart of Islam's approach to knowledge formation.⁵ In fact this is the meaning of *originality* in the Islamic perspective.

The Islamic vision of the social process has a distinctive character: it is "total", in the sense of comprehending all aspects of man's life. It is also predominantly ethical. As a result, in the Islamic perspective, it is ethics that dominate economics, and not the other way round. This view is exactly the reverse of the Marxian thesis, according to which economics are the motive force guiding man's ethical and social behaviour. This change in emphasis is not just an inconsequential interchange of words. It is absolutely fundamental to a full understanding of the "character" of Islamic economics. When the train of thought proceeds from ethics, then it is not possible to confine oneself just to illustrating and explaining socio-economic behaviour. Such an analysis must be followed up with a clear specification of the steps necessary to *correct* this behaviour in case it deviates from the prescribed ethical norms. In this framework of thought, an explanation of what *is* becomes simply a starting point of a comprehensive programme of what *ought to be*.⁶

An essential component of such a programme is the explicit recognition in Islam of the "possessive" and materialistic instincts of man: "And lo! in the love of wealth he is violent" (100:8). At the same time, true to its ethical orientation, Islam de-emphasizes these traits of human character in favour of voluntaristic altruism: "Wealth and children are an ornament of life of the world. But the good deeds which endure are better in thy Lord's sight for reward, and better in respect of hope" (18:47). Although man is free in his legitimate economic pursuits, this freedom has been duly restrained

by inculcating in man a deep sense of responsibility towards his environment. Unlike the Pythagorean scale of values according to which the life of contemplation is superior to the life of action, Islam synthesizes these two aspects of man's life into a unitary perspective in which the distinction between the secular and the spiritual is a pointless construction. It is this providential synthesis which forms the basis of social dynamics in Islam. Man should not throw up his hands in desperation and retire into the comforts of splendid isolation. He *must* act, constantly locked in battle with the forces of evil that threaten to destroy the Unity of life and the essential quality of Equilibrium. Man, instead of acting the cowardly ostrich, must face squarely the difficult problems of life. This constrained freedom, exclusive to the Islamic Message, frees man from the chains of the past and makes him the master of his destiny. As such, the maximum emphasis in Islam is on the central importance of man's discretionary powers: life does not come to a Muslim as a gigantic mechanically-operated time machine of which he is a helpless passenger; nor is it a slough of despond that he should for ever be staggering through. Instead, it appears to him as a jigsaw puzzle, whose mysteries he must keep unravelling: "We shall show them Our portents on the horizons and within themselves until it will be manifest unto them that it is the Truth" (41:53). Tirelessly exercising to the full his God-like faculty of judgement and discretion, man must fill the distinguished niche of God's vicegerency on earth. However, the powers of reason must be supported by knowledge, the acquisition of which has been made obligatory for man. Indeed, the leader-follower relationship in the Islamic perspective is based neither on age, nor on wealth, nor even on worldly power. It rests unambiguously on the superiority of knowledge and character. The Holy Qur'an elucidates this crucial point by approvingly recalling Abraham's conversation with his father: "O my father! Lo! there hath come unto me of knowledge that which came not unto thee. So follow me, and I will lead thee on a right path" (19:43).

Armed with reason and knowledge, man must go about his Divine mission of seeking to establish a society based on *al-'Adl* (i.e. Equilibrium), a quality which must hold not only at a given point of time but intertemporally as well. It is a property which must be established through a *conscious process* and not one that necessarily holds. Accordingly, the Islamic message is that the excessive concentration of income and wealth, which at present spoils the environ-

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⁶ It is somewhat paradoxical that it was Marx who had forcefully put forward the view: "Philosophers have only interpreted the world in various ways; but the real task is to alter it". However, this task of "altering" the world can be performed satisfactorily only in a non-Marxian way: through a systematic application of normative rules, with reference to which alone can the adequacy or otherwise of the present social systems be established. Furthermore, to make sure that the process of "change" does not slip into complete social anarchy and moral confusion, a set of ethical codes must *already* be there to guide social progress towards Equilibrium. The paradox lies in the fact that Marx's own materialistic vision, according to which economics hold the reins of the forces of social change, does *not* guarantee that a world changed according to his prescription will be a better world promising not only material progress but human freedom and dignity as well. The Islamic view of social dynamics does hold out such a "guarantee" through its all-embracing, unitary ethical philosophy.

thesis lies at the heart of Islam's approach to knowledge formation.⁵ In fact this is the meaning of *originality* in the Islamic perspective.

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ment in many of the Muslim countries, must be rectified by taking strong redistributive measures to restore social Equilibrium. It is interesting to note that Islam emphasized an equitable distribution of wealth several centuries before the socialists started talking about it. The philosophy of pious Muslims like Abū Dharr, who believed that to bring about *absolute* equality in income distribution was the primary duty of an Islamic state, is an eloquent proof of this assertion. Also, by focusing for the first time on the theomorphic character of man, Islam guaranteed basic human rights much earlier than they were codified in a man-made Magna Charta. In the Islamic perspective, *human freedom becomes man's inalienable right because it is God-given*. By the same token, the concentration of political power in the hands of a few individuals (i.e. oligarchy) or of the State (i.e. dictatorship) is contrary to the Islamic ideal for the simple reason that it destroys human freedom by overemphasizing Responsibility. The ultimate test of the success of Islamization will be the capacity of such an attempt to induce the best possible balance between these two elements. It is only through this route that man can attain maximum happiness in the Islamic sense of the word.

In bringing to fruition the Islamic ideal and then making people live a life according to its dictates, the State will have to play a predominant role. However there is nothing Orwellian about this conception precisely because the duties of the State in an Islamic society are limited to producing the best possible synthesis between the dictates of ethics and man's socio-economic behaviour and then translating into practice the logical consequences of such a synthesis. A State that focuses on converting ethical precepts into a viable economic programme is qualitatively different from an oppressive totalitarian regime, which suppresses basic human freedom and dignity to promote dubious social objectives, like national defence. An Islamic State worth its salt will have to focus attention on the alleviation of gross social inequalities in order to achieve Equilibrium. Only clearly-defined and ethically-conditioned social objectives can justify the various steps taken by the government to regulate economic activity in an Islamic society. In the last analysis, both the political and the economic systems rest on a definite conception of universally accepted ethical values in a particular society. Since the Islamic ethical philosophy is wedded to human freedom, no amount of socialization of the means of produc-

tion can ever degenerate into an un-Islamic totalitarian tyranny.⁷

The question may be asked at this point: is it not possible to achieve the objectives of an Islamic economy within the context of the existing economic systems, say, by opting for a welfare state? After all, it appears to be "safer" to realize the basic quality of *al-'Adl* within the framework of the economic systems already tried. Why then this rather idiosyncratic – some might even say, "irrational" – preference for a largely untried Islamic economic system, which requires taking a plunge into the unknown? The question is important and must be answered unambiguously. There are at least three main reasons why an Islamic economic system is "needed" to resolve the various social and economic problems that Muslim countries at present face. Firstly, Islam insists not only on the legitimacy of the ends but also of the means. For instance, *ribā* (i.e. a positive rate of interest) cannot be included in the set of policy instruments to tackle the monetary problems of an Islamic economy. However, while this is true, not every policy alternative to *ribā* is legitimate from an Islamic point of view. As shown clearly in Chapter 7, an economy-wide abolition of *ribā*, will entail profound *structural changes*, focusing on social justice, in the present-day economic systems. It can't be done by transplanting arbitrarily onto a capitalistic system something that clearly violates Islam's ethical philosophy. This is just one illustration of the fundamental point that the truth of the Islamic policies is strictly relative to the "Universe" of the Islamic system. Bits and pieces of the Islamic system cannot be moved at will across the spectrum of the existing economic systems. There is nothing odd about this statement, since it is the property of all "complete" systems – social, logical or mathematical – that the truth of a specific "statement" can be established only with

⁷ Even historically there is no warrant for the belief that the increasing role of the State in regulating economic life must (although it might) lead to totalitarianism. Take the case of England, Sweden, Norway and Holland where socialization and increasing government control went very far and yet none of the earlier predictions of such tendencies leading to the extinction of democratic freedoms came true. Indeed, as a result of these steps, a greater collective freedom prevails now than, for instance, during the heydays of *laissez faire* capitalism – i.e. in the wake of the 1776 Industrial Revolution in England. Actual experience has shown that both socialism and capitalism can produce economic and political servitude. All depends on the basic objectives that economic systems are supposed to serve; and, even more importantly, on the ethical values underlying these systems. If these values enshrine human freedom, as they do in Islam, then even the complete socialization of economic life cannot destroy that freedom.

reference to the system to which they belong. *The Islamic economic system rests on its distinctive ethical principles and has meaning only within this overall framework.*

Secondly, at a philosophical level, if we accept the Weberian thesis that economic behaviour is ultimately conditioned by religious beliefs, it should then not be too difficult to understand that the coexistence of incompatible religious beliefs and modes of economic behaviour is bound to end up in the smoke of intellectual and moral confusion. In fact, the artificial symbiosis of Islamic ethical beliefs and "alien" socio-economic philosophies and systems has led, in one Muslim country after another, to the emergence of "dualistic" societies, promoting schizophrenic behaviour both at the individual and at the collective level. Hence the Weberian equation between Islamic ethical beliefs and economic behaviour must be "satisfied" before the Islamization attempts can fructify.

Thirdly, even though the Islamic prescription is in broad outlines similar to what may be offered by any egalitarian economic system, the reasons for doing so are not all the same. As pointed out above, the Islamic approach to economic development does not aim at promoting material growth alone. To satisfy the dictates of Unity, it must contribute to spiritual advancement as well. This "composition" is automatically guaranteed because, in the Islamic perspective, the *ethically constrained* economic actions of man also point the way to his spiritual salvation. For instance, the act of giving (e.g. *Zakāt*) is not only a redistributive device alleviating social misery but also a means to spiritual ascent: "Ah, what will convey unto thee what the Ascent is! (It is) to free a slave, and to feed in the day of hunger an orphan near of kin, or some poor wretch in misery..." (90:12-16). The net effect of this fusion of the material and the ethical aspects in the framework of Islamic thought is to introduce a powerful element of "voluntarism" into man's economic behaviour, since the reasons for growing economically are no longer only material but spiritual as well. Needless to add, two forces acting together must be more powerful than one, even for attaining strictly materialistic objectives.

It should be noted that the view that "Islamization" should not pose any problems of immediate total acceptance by the Muslims is, to say the least, naïve. Muslims, particularly the educated élite who will count the most in making the Islamic reform take root, have been schooled in the Western value system, which, though not

necessarily bad, is different from the Islamic value system. The central point of Islamic reform will be to pull them out of the quiescent statism in which they find themselves stuck, sitting listlessly in the dark shadows of material deprivation and deliquescent spiritual decadence. A large body of dispirited Muslims with their creative faculties held in intellectual captivity, have been guided for centuries by a herd instinct. Such an attitudinal straitjacket will have to be cast off. A slavish mimesis of "alien" thoughts must give way to bold and imaginative initiatives in the realm of ideas. Nothing short of a "re-education" process will be required to wean away the Muslims from their "traditional" habits of thought.⁸

The Muslims will have to get accustomed to a societal framework in which human freedom is ethically constrained and selfishness is not accepted as a virtue. In the process of getting to know Islam, man's social consciousness, through a deep conviction of social responsibility, will have to be considerably "expanded". For men in an Islamic society to suppress a mechanical, and essentially irrational, reaction behaviour of going from one extreme to another cannot be easy. Such behaviour will have to be replaced, even at the intellectual plane, with a conscious effort to always stick to the "middle course". The Holy Qur'ān is explicit on the decisive character of man-made decisions as determinants of social progress: "... Allah never changeth the grace He hath bestowed on any people until they first change that which is in their hearts ..." (8:53). No aimless gadabouts in an intellectual wilderness, Muslims will have to anchor their thought processes to a perspective of certitude and equilibrium. Furthermore, in an Islamic system, man will have to learn to be proud of his theomorphic potentialities to keep him in touch with his environment, indeed with the universe around him. He would then suffer no "alienation" — as he does under capitalism, according to Marx — even in the darkest hour of loneliness, dejection and isolation. To bring about such profound attitudinal changes will take nothing less than a moral revolution.

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For the Islamization process to succeed, a "populist" approach, involving a society-wide mobilization, will be required. Here we have the politico-economic element of the "transition period". It is essential that the reformist's emphasis should be on implementing the Islamization programme in terms of the broad social objectives based on the Islamic ethical axioms. As pointed out above, the Islamic "bias" is towards the economically weak. No condescending patronization of the poor by the rich will be acceptable to an Islamic society. As a matter of social policy, a complete reorganization of the social structure will be required to move men towards a social Equilibrium. That would require catapulting the poor along the social ladder while pushing down the rich, in line with the Qur'anic commandment: "... Whoso is rich, let him abstain generously ...; and whoso is poor let him take thereof in reason" (4:6). The quality of Equilibrium must be satisfied not only horizontally but also vertically. In to-day's terminology, such a programme may appear an extreme "leftist" philosophy to those who are in the habit of putting every new idea into a carefully labelled box. It is significant that Islam unequivocally rejects such a label and instead calls its middle-of-the-road programme the "straight path" of social harmony and moral rectitude.

However, the success of the Islamization process will depend crucially on the exact strategy followed for realizing the basic objectives of an Islamic society; in particular by the measures taken to initiate the long and arduous journey towards the Islamic ideal. It is absolutely essential that we *begin* by taking decisive measures to change into the Islamic mould the unjust and the oppressive social structures now prevalent in the Muslim countries, and not by emphasizing symbolic gestures and empty slogans, tooting horns and waving flags. The process of Islamization will be aborted unless the pockets of vested interest are effectively eliminated. Only then will a "fluid" social structure come into being, free of iniquitous and oppressive rigidities. The superiority of the Islamic solution over the capitalistic and socialistic solutions will ultimately be established mainly by its success in ensuring social justice with human dignity. It is what Islam stands for and does for human happiness that will finally decide the outcome of the Islamic resurgence in Muslim countries. The Islamic world is going through the pangs of a rebirth into a modern world which is at once difficult and complex and additionally is not fully prepared to accept the final "event".

It is a challenge of the first order that Muslim social philosophers face. Their mettle will be tested by their willingness to go through the ordeal that every challenge brings in its train, persist with it and come out with answers which are both Islamically legitimate and acceptable to the modern mind. This is not an easy task but it must be accomplished to turn the winter of our discontent into a full-blown spring.

One may ask: "if winter comes, can spring be far behind"? Will history not repeat the glory of the Muslims that was theirs? It might, but it is not a natural necessity. In the Islamic perspective, it is only through conscious action, supported by faith, that we can pull ourselves out of the morass of moral defeat. It all depends on our ability to arrest effectively the progressive drift of the Muslim societies to the edge of a precipice and our refusal to surrender our souls to the blinding forces of materialism. How can this be done? Not with iron in our souls but by reasserting our theomorphic character, informing our thoughts with a sense of the sacred, and aligning ourselves with the all-comprehending Unity that lords over the Universe.⁹ This "strategy" alone can produce order and harmony in our lives, which are at present benighted by shattered dreams and forlorn hopes. Through its unitary philosophy Islam seeks to guide man through the labyrinths of a life which has been broken up into incongruous bits and pieces under the stress of a strident materialism. Its mission is to restore man to his "primal" theomorphic place where life is a homogeneous whole, and to imbue him with courage, moral strength and spiritual happiness. The success of such a momentous mission will require the creation of an environment where human freedom flowers and finds new avenues for creative self-fulfilment. However, the Islamic free man is not the "mootless" and "lawless" Homeric Cyclop who lives "in sovereign disregard of all his peers",¹⁰ but is a responsible human being, deeply sensitive to the injustices of his

⁹ It may be interesting to note that Toynbee characterizes an "active response" to the forces of social disintegration as "an awakening to a sense of Unity which broadens and deepens as the vision expands from the Unity of mankind, through the Unity of the cosmos, to embrace the Unity of God" [5, p. 431]. This is exactly what Islam does: to promote a perspective of certainty by asking man to focus on the Unity of God. However, in the Islamic perspective the chain of causation is exactly the reverse of what Toynbee prescribes: It proceeds from *belief* in the Unity of God, to the Unity of the cosmos and then finally to the Unity of mankind and going a step further to the Unity of man's social and economic behaviour.

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¹⁰ Quoted from Homer's *Odyssey* in Toynbee [5, p. 209].

environment *and* doing his utmost to correct them. As Muslims experience an uncommon exhilaration and unbounded delight at the sweeping pageant of the Islamic revival throughout the world, they should not lose sight of the immense challenge that this phenomenon poses. To react creatively to this momentous challenge is the task Muslims face.

With every opportunity there comes a thousand temptations. The calibre of individuals and nations is measured by their ability to make correct judgements in the hour of trial, distinguishing between the opportunity and the temptations. The present resurgence of Islam in a world of material affluence and moral turpitude offers a great opportunity to Muslims to change their "traditional" modes of thought radically since the compartmentalization of life made fashionable by the modern age will have to be undone in an Islamic society. Their success in this Herculean task will depend, however, on the extent to which they perceive the nature and the significance of this challenge and act accordingly. Once the direction and magnitude of the process of "Islamization" of the society have been determined, an appropriate institutional framework, *which is neither socialistic nor capitalistic but distinctly Islamic*, will have to be developed to redirect the immense social forces released by the explosion of expectations about what Islam can do for the happiness of mankind. A societal reordering carried out on the basis of Islam's four basic ethical precepts will be Islam's gift not only to Muslims but to all well-meaning humanity. Its unitary philosophy offers an effective way out of the tragedy of the modern world, which glorifies the pointless dichotomy between man's ethical beliefs and his economic behaviour. The Islamic message is addressed to those who like order and symmetry in their lives but, in the absence of a satisfactory philosophy, keep on enduring an inner split between the call of the flesh and the beckoning of the soul. It should make no sense to them that, while the noise and the bustle of the world never reach the cloisters of the spiritualists, floating weightlessly in a sleepy hollow, they bury the materialistic grabber in an abysmal confusion. For such people the choice of the Islamic ideal will be the choice of freedom, contributing to social harmony and world peace. Once this is fully realized by non-Muslims, the entire world, not Muslims alone, will have a "vested" interest in the success of the Islamic resurgence. For how can the world remain cool to a social philosophy which guaranteed human freedom with a correct emphasis on

responsibility, obliterated schizophrenic mix-up by emphasizing the essential Unity of human existence, and relieved social tensions by ignoring class conflicts and re-establishing social Equilibrium.

If the Islamic Reform, the outlines of which have been sketched with a broad brush in these pages, is implemented in both letter and spirit, all talk of a "militant Islam" on the march for yet another Crusade will appear to well-meaning people, to whom alone this book is addressed, as both pointless and irrelevant. There can be no better indication of our intentions than the example we set for the whole world by our deeds. The sincerity of the purpose of honest men of thought and action alone will crown the Islamic Reform with success. It is easy for those who employ the motives of virtue as the instruments of their ambition to revive the dying ember of faith with the breath of fanaticism, but much more will be required to turn it into a shaft of light that scatters the darkness of ignorance and poverty and human degradation. The Islamic ideal is calm and generous, free from passional suffocations and sterile disputes about words. To achieve it, habits of deep thought and reflection on God's Universe will have to replace mediocrity and the search for mechanical and ready-made solutions; or else, the momentum of Islamization will wither on the vine through sheer lack of an appropriate response from Muslims to the great challenge they face. Not a mere veneer or a masquerade masking non-Islamic motives, but an earnest effort to translate words into a concrete programme of action, will have to be the Muslims' answer to the challenge of Islamic resurgence. Nature is never tired of presenting new mysteries to challenge human ingenuity since the act of creation is a continuous process. "See they not how Allah produceth creation, then reproduceth it?" (29:19). Or else, the world will cease to exist; and so would end man's role as God's viceroy on Earth. Till such time, the search must go on for the ultimate truth, not by raking up the ashes of an irrelevant past, but by venturing forth in search of new horizons in the spirit of pioneers and pace-setters, with the providential assurance, "I suffer not the work of any worker, male or female, to be lost" (3:195).

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